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SECURITIES REGULATION — TENDER OFFER — CONDUCT IN CONNECTION WITH A TENDER OFFER REQUIRES AN ELEMENT OF DECEPTION TO BE CONSIDERED MANIPULATIVE UNDER SECTION 14(E) OF THE WILLIAMS ACT. *Schreiber v. Burlington Northern, Inc.*, 731 F.2d 163 (3d Cir. 1984).

In *Schreiber v. Burlington Northern, Inc.*,[1] the United States Court of Appeals for the Third Circuit[2] held that conduct in connection with a tender offer[3] is not a prohibited "manipulative"[4] act within the meaning of Section 14(e) of the Securities Exchange Act of 1934[5] unless it contains an element of deception. The court predicated its conclusion primarily upon its interpretation of the Congressional intent[6] behind amending the Securities Exchange Act of 1934[7] with the Williams Act.[8] By holding that manipulative acts must in-

1. 731 F.2d 163 (3d Cir. 1984).

2. The Third Circuit panel was composed of Judges Adams, Sloviter, and Teitelbaum. Judge Adams delivered the opinion of the court.

3. The term "tender offer" has not been officially defined by either Congress or the Securities and Exchange Commission, but a House report has broadly described the term as follows:

> The cash tender offer has become an increasingly favored method of acquiring control of publicly held corporations. The offer normally consists of a bid by an individual or group to buy shares of a company — usually at a price above the market price. Those accepting the offer are said to tender their stock for purchase. The person making the offer obligates himself to purchase all or a specified portion of the tendered shares if certain specified conditions are met.

H.R. REP. NO. 1711, 90th Cong., 2d Sess. *reprinted in* 1968 U.S. CODE CONG. & AD. NEWS 2811. For a more detailed discussion of what constitutes a tender offer, see generally Note, *Toward A Definition of "Tender Offer"*, 19 HARV. J. ON LEGIS. 191 (1982); Note, *What is a Tender Offer?*, 37 WASH & LEE L. REV. 908 (1980).

4. *See infra* note 45.

5. 15 U.S.C. § 78n(e) (1982). This section states as follows:

> (e) Untrue statement of material fact or omission of fact with respect to tender offer
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> It shall be unlawful for any person to make any untrue statement of material fact or omit to state any material fact necessary in order to make the statements made, in the light of the circumstances under which they are made, not misleading, or to engage in any fraudulent, deceptive, or manipulative acts or practices, in connection with any tender offer or request or invitation for tenders, or any solicitation of security holders in opposition to or in favor of any such offer, request, or invitation. The Commission shall for the purposes of this subsection, by rules and regulation define, and prescribe means reasonably designed to prevent, such acts and practices as are fraudulent, deceptive, or manipulative. [hereinafter cited as Section 14(e)].

6. *See infra* note 32 and accompanying text.

7. 15 U.S.C. §§ 78a-78kk (1982).

8. 15 U.S.C. §§ 78m(d)-(e), 78n(d)-(f) (1982).

clude an element of deception,[9] the Third Circuit has involved itself in an ongoing debate within the legal community[10] as to the role federal courts should play in determining the substantive fairness of tender offers.

During December 1982, R-H Holdings Corporation and its parent corporation,[11] Burlington Northern Inc., planned to usurp corporate control of the El Paso Gas Company by purchasing a majority interest in El Paso common stock. On December 21, 1982, R-H publicly announced a tender offer for 25,100,000 shares[12] of El Paso common stock at twenty-four dollars per share — a price well above the then current rate. The offer, however, was subject to R-H's right to withdraw prior to accepting any share for payment.[13] Although El Paso shareholders fully subscribed to the tender offer before its December 30, 1982 deadline, R-H decided to exercise its option to withdraw. This decision resulted from an accord between R-H, Burlington, and El Paso. After initially countering the takeover bid with a variety of defensive measures,[14] El Paso's management decided to negotiate with R-H and Burlington. The parties reached an agreement and publicly disclosed it on January 10, 1983. In exchange for

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9. *Schreiber*, 731 F.2d at 166.

10. *See* Note, *Target Defensive Tactics as Manipulative Under Section 14(e)*, 84 COLUM. L. REV. 228, 231-34 (1984) (surveys judicial opinions which differ in their interpretation of Section 14(e)).

11. R-H Holdings Corp. is a wholly owned subsidiary of Burlington Northern, Inc. Schreiber v. Burlington Northern, Inc., 568 F. Supp. 197, 199 (D. Del. 1983). *See generally* N. LATTIN, THE LAW OF CORPORATIONS 90-96 (1959) (provides a general discussion of parent and subsidiary corporate relationships).

12. The number of shares requested by R-H in the first tender offer constituted a slight majority of El Paso's common stock. *Schreiber*, 568 F. Supp. at 199.

13. The provision by which R-H preserved its right to withdraw the tender offer was worded as follows:

> Notwithstanding any other provision of the Offer, the Purchaser shall not be required to accept for payment or pay for tendered Shares, or may terminate or amend the Offer . . . if, at any time on or after December 17, 1982 and prior to the acceptance for payment of any such Shares . . ., any of the following shall occur: . . . if, in the sole judgment of the Purchaser, in any such case, regardless of the circumstances (including any action or inaction by the Purchaser) giving rise to any such condition, such condition makes it inadvisable to proceed with the Offer and/or with such purchase or payment.

Id.

14. A defensive measure is any action undertaken by the management of a corporation to discourage or prevent a takeover attempt by another corporation. *See* Note, *supra* note 10, at 229. For a thorough discussion of the variety of defensive measures utilized by corporations, see generally A. FLEISCHER, TENDER OFFERS: DEFENSES, RESPONSES AND PLANNING 113-55 (1978); E. ARANOW, H. EINHORN & G. BERLSTEIN, DEVELOPMENTS IN TENDER OFFERS FOR CORPORATE CONTROL 193-206 (1977); Easterbrook & Fischel, *The Proper Role of a Target's Management in Responding to a Tender Offer*, 94 HARV. L. REV. 1161 (1981).

El Paso's management countered R-H's tender offer by filing suits against R-H and Burlington in both the Delaware Court of Chancery and the United States District Court for the Northern District of Texas. El Paso informed the Securities and Exchange Commission that it planned to dispose of its assets. El Paso also issued a new class of preferred stock and amended its corporate by-laws. *Schreiber*, 568 F. Supp. at 199.

golden parachute contracts,[15] El Paso management agreed to cease opposing the takeover attempt. In addition, R-H withdrew its original tender offer in favor of a second, smaller offer. The second tender offer requested only twenty-one million shares at twenty-four dollars per share. R-H agreed to purchase directly from El Paso the additional shares it needed to acquire a majority interest.[16]

El Paso shareholders reacted very favorably to the second tender offer. The shares tendered greatly exceeded the amount requested,[17] and, as a consequence, R-H could only accept a certain percentage of each individual's tendered shares.[18] El Paso stockholders who tendered shares under both offers, suffered financially from the withdrawal of the original offer. Able to sell the full amount of their shares under the original offer, they now were entitled to sell only a portion of their shares.[19] Barbara Schreiber, one such stockholder, brought an action for damages on behalf of herself and others similarly situated, in the United States District Court for the District of Delaware against El Paso, El Paso's directors, Burlington, and R-H.[20] She alleged two separate violations of Section 14(e). First she contended that the withdrawal of the original tender offer in favor of a second was a manipulative act prohibited by Section 14(e). Second she argued that failure to reveal the contracts given to certain El Paso directors was a transgression of Section 14(e)'s disclosure requirement.[21]

At trial, the defendants moved to dismiss the plaintiff's complaint for "failure to state a claim upon which relief can be granted."[22] In granting the motion, the district court concluded that Ms. Schreiber failed to state a claim for violation of Section 14(e) because she neglected to allege, under either theory, that damages had resulted from the purported deception.[23] On appeal, the Third Circuit, while addressing both allegations of the plaintiff, dealt primarily with the question of whether Section 14(e)'s phase "manipulative acts or practices" encompassed activity not involving

15. "So-called 'golden parachutes' generally provide multi-year benefits to high level executives of a target company after a takeover if they are discharged without cause or downgraded by the new management." *Schreiber*, 731 F.2d at 165 n.2. *See generally* SHARK REPELLENTS AND GOLDEN PARACHUTES 425-36 (R. Winter, M. Stumpf, & G. Hawkins ed. 1983) (addresses definition, structure, and purpose of "golden parachute" agreements).

16. The defendant directors, who had not tendered their shares in the original offer, would be able to tender their shares during the second offer. *Schreiber*, 568 F. Supp. at 200.

17. The tender offer requested only 21 million shares, but over 40 million shares were tendered. *Schreiber*, 731 F.2d at 165.

18. The Williams Act requires pro rata acceptance of shares in tender offers that are over subscribed. *See* 15 U.S.C. § 78n(d)(6)(1982).

19. *See supra* note 18.

20. *Schreiber*, 731 F.2d at 165.

21. *Id.*

22. FED. R. CIV. P. 12(b)(6).

23. *Schreiber*, 731 F.2d at 164.

deception.[24]

In 1968 the Williams Act[25] was enacted as an amendment to the Securities Exchange Act of 1934[26] to expand the protection provided by federal law for individuals who invest funds in corporate securities.[27] Three sections[28] of the Williams Act set forth the requirements that must be fulfilled when making a tender offer[29] — a method of achieving corporate control that achieved widespread popularity during the 1960's.[30] In contrast to other methods of acquiring corporate control,[31] tender offers were not subject to federal securities law prior to 1968. Congress passed the Williams Act[32] primarily to remove this gap in investor protection.

Section 14(e),[33] one of the tender offer sections, is a "broad antifraud provision"[34] patterned in large measure upon Securities and Exchange Commission Rule 10b-5.[35] The section prohibits any

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24. *Id.* at 164.

25. Pub. L. No. 90-439, 82 Stat. 454 (amended 1970) (codified as amended at 15 U.S.C. §§ 78m(d)-(e), 78n(d)-(f) (1982)). Sections 13(d), 13(e), 14(d), 14(e), and 14(f) were amended to the Securities Exchange Act of 1934 by the Williams Act.

26. 15 U.S.C. §§ 78a-78kk.

27. 113 CONG. REC. 854-56 (1967) (statement of Sen. Williams, co-sponsor of the legislation). *See also infra* note 32.

28. 15 U.S.C. §§ 78n(d)-(f) (1982).

29. *See supra* note 4.

30. In 1960 only eight tender offers occurred, but in 1966 the number of tender offers increased to over one hundred. The rapid growth in popularity was due primarily to the speed with which a tender offer can be executed. A tender offer can often be successfully completed in a matter of days. 113 CONG. REC. 24664 (1967) (statement of Sen. Williams).

31. *See generally* 15 W. FLETCHER, FLETCHER CYCLOPEDIA OF THE LAW OF PRIVATE CORPORATIONS §§ 7040-46.1 (1983) (discussion of mergers, consolidations, and combinations as devices by which one corporation attains control over another).

32. "This legislation [Williams Act] will close a significant gap in investor protection under the Federal Securities laws by requiring the disclosure of pertinent information to stockholders when persons seek to obtain control of a corporation by a cash tender offer . . . ." 113 CONG. REC. 854 (1967) (statement of Sen. Williams).

33. Section 14(e) was amended by the Act of Dec. 22, 1970, § 2, 84 Stat. 1497 (1970) (codified as amended at 15 U.S.C. § 78n(e) (1982)). The amendment, which added the final sentence to the current Section 14(e), provided the Securities and Exchange Commission with rulemaking power to prohibit acts which it deemed to be within the scope of the section. Senator Williams, author of both the original Section 14(e) and its amended version, described the purpose of the amendment as follows:

> The third change which this proposed legislation would make in existing law would be to give the Securities and Exchange Commission rulemaking power with respect to fraudulent, deceptive and manipulative activities made in connection with a tender offer.
>
> This provision is of the utmost necessity. The techniques used in corporate takeovers have become increasingly sophisticated and change rapidly. This is particularly true in situations where the takeover is resisted by incumbent management — industrial warfare develops. Claims and counterclaims, charges and countercharges are hurled back and forth. Efforts are often made to influence the price of the securities involved. The Commission must be given full rulemaking powers to deal with these rapidly changing problems.

116 CONG. REC. 3024 (1970) (statement of Sen. Williams).

34. Panter v. Marshall Field & Co., 646 F.2d 271, 283 (7th Cir. 1981), *cert. denied*, 454 U.S. 1092 (1981).

35. 17 C.F.R. § 240.10b-5 (1982). *See infra* notes 80-82 and accompanying text.

fraudulent, deceptive, or manipulative act or practice in connection with a tender offer. Unfortunately, however, section 14(e) itself neither explains nor defines the meaning of fraudulent, deceptive, or manipulative.[36] This failure to clearly distinguish between the types of conduct covered by its language has resulted in a judicial controversy concerning whether the presence of deception is always required in establishing the existence of a manipulative act.[37]

Mobil Corp. v. Marathon Oil Co.[38] was the first case to consider what constituted a manipulative act under Section 14(e).[39] In *Mobil*, the United States Court of Appeals for the Sixth Circuit[40] held that a corporation's lock-up[41] and stock options,[42] which were employed to counter a takeover bid, comprised manipulative activity under Section 14(e) despite the absence of deception by the corporation. The Sixth Circuit presented four reasons for rejecting the contention that manipulative acts in tender offers must include deception. First, the interpretation of the term "manipulative" must be flexible to incorporate any new tactics or techniques[43] for acquiring corporate control that might arise in the rapidly changing securities field.[44] Second, the judicial history of the concept of manipulation in relation to corporate securities[45] suggests that the term should in-

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36. *See Section 14(e), supra* note 5.

37. *See generally* Weiss, *Defensive Responses to Tender Offers and the Williams Act's Prohibition Against Manipulation*, 35 VAND. L. REV. 1087, 1095-98 (1982) (commentator analyzes the language of Section 14(e) in light of the history of the term "manipulation" in securities law).

38. 669 F.2d 366 (6th Cir. 1981).

39. *Schreiber*, 731 F.2d at 165.

40. *Mobil*, 669 F.2d at 375.

41. The term "lock-up" describes a defensive tactic often utilized when two corporations are vying for control of a third corporation by use of competing tender offers. The threatened corporation enters an agreement with one of the attacking corporations providing that corporation with certain advantages designed to discourage or thwart the other corporation's takeover attempt. Note, *"Lock-up" Enjoined Under Section 14(e) of Securities Exchange Act*, 12 SETON HALL 881, 882 (1982). *See generally* Note, *The Future of Lock-ups after Mobil v. Marathon Oil*, ST. LOUIS U.L.J. 261, 264-266 (1983) (describes the advantages and disadvantages of the lock-up as a device to prevent takeover attempts).

Mobil Oil Co. and United States Steel Corp. were both attempting to takeover Marathon Oil. Marathon granted U.S. Steel a lock-up option, which provided that U.S. Steel would have the right to buy Marathon's most valuable asset, the Yates Oil Field, if its tender offer failed to gain a majority of Marathon's common stock. Marathon hoped Mobil would be dissuaded from its takeover attempt since a victory in the tender offer contest with U.S. Steel would not provide access to Marathon's prime asset. *Mobil*, 669 F.2d at 367.

42. U.S. Steel was granted a present, irrevocable right to purchase 10 million authorized but unissued shares of Marathon common stock, which constituted approximately 17 percent of Marathon's outstanding shares. *Id.*

43. *See supra* note 33.

44. *Mobil*, 669 F.2d at 374.

45. Hundahl v. United Benefit Life Ins. Co., 465 F. Supp. 1349, 1359-61 (N.D. Tex. 1979) discusses the history of the term "manipulation" in the context of securities from its origin in English common law to the adoption of the Securities Exchange Act of 1934. The court concluded that the term "manipulation" was intended to encompass any activity interfering with the workings of securities markets by misleading investors or distorting prices. *See also* 3 L. LOSS, SECURITIES REGULATION 1529-70 (2d ed. 1961) (concludes that the English

clude any deliberate conduct intended to harm investors by "controlling or artificially affecting the price of securities."[46] Third, since Congress' essential purpose in drafting the Williams Act was the protection of shareholders confronted with a tender offer[47] all activities that could adversely affect the ability of shareholders to maximize their earnings should be classified as manipulative under Section 14(e). Requiring only mere disclosure under the statute would defeat congressional intent since publicly disclosed activities damaging to the interests of investors would not fall within the scope of Section 14(e).[48] Last, to require the presence of deceptive activity to establish manipulation would effectively erase manipulative acts and practices as a separate category under Section 14(e). The section's separate classification of deceptive and manipulative activity would be unnecessary since deception would be required in both instances.[49]

The *Mobil* opinion has not been favorably received by other federal courts.[50] Though not addressing the manipulation question, several courts[51] have differed with *Mobil's* interpretation of the congressional purpose underlying the Williams Act and Section 14(e). Decisions from several other federal courts, of which *Schreiber* is the most recent, have directly contradicted the holding of *Mobil*.[52]

In *Martin Marietta Corp v. Bendix Corp.*,[53] the United States District Court for the District of Maryland[54] held that a corporation's use of a counter tender offer[55] to thwart another corporation's takeover bid was not a manipulative act in violation of Section 14(e).

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common law concept of manipulation as any activity interfering with the free market mechanism was incorporated by the Securities Exchange Act of 1934).

46. *Mobil*, 669 F.2d at 374 (citing Ernst & Ernst v. Hochfelder, 425 U.S. 185, 199 (1976)).

47. *Mobil*, 669 F.2d at 376.

48. *Id.* at 376-77.

49. *Id.*

50. Pacific Realty Trust v. APC Investments, Inc., 685 F.2d 1083 (9th Cir. 1982) is the only federal circuit decision that has endorsed the interpretation of Section 14(e) adopted by *Mobil*. "There are instances where violations of this antifraud provision [Section 14(e)] are unrelated to the information supplied to the shareholders." *Id.* at 1086. The court, however, found no activity warranting application of *Mobil* in the case before it. *Id.*

51. *See, e.g.*, Dan River, Inc. v. Icahn, 701 F.2d 278, 288 (4th Cir. 1983) (sole purpose of Section 14(e) is to ensure adequate disclosure to shareholders who are deciding whether to tender their shares); *Panter*, 646 F.2d at 283 (Section 14(e) designed to ensure that shareholders who are confronted with a tender offer have adequate and accurate information); Lewis v. McGraw, 619 F.2d 192, 195 (2d Cir. 1980), *cert. denied*, 449 U.S. 951 (1980) (Section 14(e) intended to ensure that investors will not have to respond to a tender offer without adequate information).

52. *Schreiber*, 731 F.2d at 164 (notes several previous decisions criticizing the *Mobil* holding). *See infra* notes 61 and 65.

53. 549 F. Supp. 623 (D. Md. 1982).

54. *Id.* at 627-28.

55. In response to Bendix's tender offer for Marietta shares, Martin Marietta responded with its own tender offer for Bendix shares. The district court described this activity as a "Pac-Man struggle" since each corporation was attempting to engulf the other. *Id.* at 625.

Employing an exhaustive analysis of both legislative history and prior judicial opinions,[56] the district court concluded that the underlying purpose of the Williams Act is protection of investors confronted with a tender offer by assuring full and fair disclosure of pertinent information.[57] Any action brought under Section 14(e), including a claim alleging manipulative acts, thus, must demonstrate that the corporate entities involved have either disseminated false data or withheld relevant information.[58]

In two 1983 cases[59] decided several months apart, the United States Court of Appeals for the Second Circuit[60] also held that deception is a necessary element of manipulative acts under Section 14(e). In *Buffalo Forge Co. v. Ogden Co.*,[61] the Second Circuit[62] held that a corporation's scheme to counter a takeover bid by publicly seeking a white knight[63] was not manipulation. In *Data Probe Acquisition Corp. v. Datalab, Inc.*,[64] the Second Circuit[65] held that a right to buy stock given by one corporation to another to thwart a tender offer by a third corporation was not a manipulative act. In each case, the court grounded its holding on the observation that the primary purpose behind the tender offer legislation was the protection of shareholders through adequate disclosure of financial information. The court noted that Section 14(e) is designed to ensure that the investor has adequate information upon which to make an intelligent investment decision.[66] In *Buffalo*, the Second Circuit also noted that the business judgment[67] of the threatened corporation's direc-

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56. *Martin* relies primarily on Piper v. Chris-Craft Indus., 430 U.S. 1 (1977), which extensively analyzed the legislative history of the Williams Act. The Supreme Court noted, "The sponsors of this legislation [Williams Act] were plainly sensitive to the suggestion that the measure would favor one side or the other in control contests; however, they made it clear that the legislation was designed solely to get needed information to the investor, the constant focal point of the committee hearings." *Id.* at 30-31.

57. *Martin*, 549 F. Supp. at 627-28.

58. *Id.* at 628.

59. *See infra* notes 61 and 64.

60. *See infra* notes 62 and 65 and accompanying text.

61. 717 F.2d 757 (2d Cir. 1983), *cert. denied*, 104 S. Ct. 550 (1984).

62. *Id.* at 760.

63. The term "white knight" is used in connection with a defensive tactic used by a corporation threatened with a hostile takeover. A corporation may attempt to thwart the takeover bid by merging with a corporation of its choice. The friendly corporation is dubbed a white knight. Lynch & Steinberg, *The Legitimacy of Defensive Tactics in Tender Offers*, 64 CORNELL L. REV. 901, 931 (1979). *See also* Profuser, *Tender Offer Manipulation: Tactics and Strategies after Marathon*, 36 Sw. L.J. 975, 981 n.52 (1982) (merger agreements between a corporation and a white knight are intended to rebuff unwanted tender offers).

64. 722 F.2d 1 (2d Cir. 1983), *cert. denied*, 104 S. Ct. 1326 (1984).

65. *Id.* at 4.

66. *Compare Data Probe*, 722 F.2d at 4 (notes that misrepresentation is an essential element of a Section 14(e) cause of action) *with Buffalo*, 717 F.2d at 760 (states that an essential ingredient of a Section 14(e) cause of action is the omission or misstatement of material facts).

67. Actions by corporate directors are often protected by the Business Judgment Rule, which "sustains corporate transactions and immunizes management from liability where the

tors should not be disturbed since its stockholders received greater remuneration[68] due to the directors' actions.[69]

In *Data Probe*, the goal of maintaining the distinction between state substantive corporate law and federal securities law greatly influenced the court's reasoning.[70] Although acknowledging that the actions of certain corporate directors could possibly be a violation of the fiduciary duty owed to shareholders,[71] the Second Circuit refused to extend the coverage of Section 14(e) to an area traditionally regulated by state law.[72]

Relying on both *Buffalo* and *Data Probe*,[73] *Schreiber* provides the most recent criticism of the *Mobil* holding.[74] According to *Schreiber*, both the legislative history[75] and the United States Supreme Court interpretation[76] of the Williams Act establish that the Act was "designed to make relevant facts known so that shareholders have a fair opportunity to make their decisions."[77] Section 14(e) of the Williams Act, therefore, was not enacted to provide a federal cause of action for any harm suffered in connection with a tender offer. Rather, Congress intended Section 14(e) merely to ensure that sufficient information would be available to investors confronted with a tender offer. Section 14(e) prohibits only activity that is designed

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transaction is within the powers of the corporation and the authority of management, and involves the exercise of due care and compliance with applicable fiduciary duties." HENN & ALEXANDER, LAW OF CORPORATIONS 661-63. *See generally* Prentice, *Target Board Abuse of Defensive Tactics: Can Federal Law Be Mobilized to Overcome the Business Judgment Rule?*, 8 J. OF CORP. L. 337 (1983) (analyzes the inherent conflict of interest between the management and shareholders of a corporation confronted with a tender offer and the effect it could have on the Business Judgment Rule).

68. The tender offer price for shares rose from $25.00 to $37.50 per share. *Buffalo*, 717 F.2d at 759.

69. *Id.*

70. Cort v. Ash, 422 U.S. 66 (1975) aptly described the distinction between state and federal corporation law: "Corporations are creatures of state law, and investors commit their funds to corporate directors on the understanding that, except where federal law expressly requires certain responsibility of directors with respect to stockholders, state law will govern the internal affairs of the corporation." *Id.* at 84.

71. Northwest Indus., Inc. v. B.F. Goodrich Co., 301 F. Supp. 706 (N.D. Ill. 1969) provides a succinct statement of corporate management's fiduciary duty. The court stated:

> [M]anagement has the responsibility [under state law] to oppose [tender] offers which, in its best judgment, are detrimental to the company or its stockholders. In arriving at such a judgment, management should be scrupulously fair in considering the merits of any proposal submitted to its stockholders. The officers' and directors' informed opinion should result from that strict impartiality which is required by their fiduciary duties. After taking these steps, the company may then take any step not forbidden by law to counter the attempted capture.

Id. at 712-13. *See also* Henn & Alexander, *supra* note 67, at 625-28.

72. *Data Probe*, 722 F.2d at 6.

73. *Schreiber*, 731 F.2d at 165.

74. *See supra* note 40 and accompanying text.

75. *See supra* note 32.

76. *E.g.*, Rondeau v. Mosinee Paper Corp., 422 U.S. 49, 58 (1975) (sole purpose of Williams Act is to ensure that an investor is provided with needed information).

77. *Schreiber*, 731 F.2d at 166 n.3 (citing H.R. REP. NO. 1711, 90th Cong., 2d Sess., *reprinted in* 1968 U.S. CODE CONG. & AD. NEWS 2811, 2813).

to either mislead or deceive shareholders faced with a tender offer.[78] All acts prohibited by Section 14(e), including those described as manipulative, must therefore embody an element of deception.[79]

The *Schreiber* court's conclusion that Section 14(e) compels only information disclosure also relies on the Supreme Court's analysis[80] of the term "manipulative device" found in Securities and Exchange Commission Rule 10b-5[81] — a rule extremely similar to Section 14(e) in both wording and effect.[82] In *Santa Fe Industries, Inc. v. Green*, the high court narrowly defined manipulative device to include only conduct designed to mislead investors by artificially affecting the securities market.[83] Applying this definition to the manipulation claim before it, the Third Circuit concluded that manipulative acts must always involve deceit or nondisclosure.[84]

The *Schreiber* court was also concerned about the impact that a broad construction of the section would have on the traditional relationship between federal and state law.[85] The court admitted that Section 14(e)'s language was sufficiently ambiguous to cause reasonable differences of opinion about its scope since the section specifically prohibits both deceptive and manipulative acts.

Inclusion of both categories within the statute could arguably be construed as indicating that Congress intended to regulate more than just deceptive conduct.[86] Although adopted by *Mobil*,[87] this rationale

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78. *Schreiber*, 731 F.2d at 165-66.

79. *Id.* at 166.

80. *See* Santa Fe Indus., Inc. v. Green, 430 U.S. 462 (1977); Ernst & Ernst v. Hochfelder, 425 U.S. 185, 199 (1976).

In *Santa Fe*, the Supreme Court stated that in the context of SEC Rule 10b-5 the term "manipulative" encompasses any "action" affecting market activity in order to mislead investors." *Santa Fe*, 430 U.S. at 477. In *Ernst*, the court noted, "[Manipulation under SEC Rule 10b-5] connotes intentional or willful conduct designed to deceive or defraud investors by controlling or artificially affecting the price of securities. *Ernst*, 425 U.S. at 199.

81. 17 C.F.R. § 240.10b-5 (1982).

> Employment of manipulative and deceptive devices.
>
> It shall be unlawful for any person, directly or indirectly, by the use of any means or instrumentality of interstate commerce, or of the mails or of any facility or of any national securities exchange,
>
> (a) To employ any device, scheme, or artifice to defraud,
>
> (b) To make any untrue statement of a material fact or omit to state a material fact necessary in order to make the statements made, in the light of the circumstances under which they were made, not misleading, or
>
> (c) To engage in any act, practice, or course of business which operates or would operate as a fraud or deceit upon any person, in connection with the purchase or sale of any security.

82. "Section 14(e) is a somewhat unique case of a statute patterned after a regulation; it tracks in large measure the language [of] Rule 10b-5." *Hundahl*, 465 F. Supp. at 1336. *See also* Atchley v. Qonaar Corp., 704 F.2d 355, 358 (7th Cir. 1983) (notes that Section 14(e)'s language is patterned after Rule 10b-5); *Panter*, 646 F.2d at 283 (states that Section 14(e) is modeled after Rule 10b-5).

83. 430 U.S. at 1302. *See also supra* note 80.

84. *Schreiber*, 731 F.2d at 166.

85. *Id.*

86. *Id.*

was rejected by *Schreiber*.[88] In the *Schreiber* court's view if the definition of manipulative acts did not include an element of deception federal courts would be called to assume jurisdiction of litigation involving questions concerning the substantive propriety of tender offers.[89] This would result in the federalization of a large segment of corporate law, traditionally a state matter.[90] The Third Circuit in *Schreiber* refused to embark on this radical course of action.[91]

The plaintiff's second theory of recovery, which alleged a deceptive act in violation of Section 14(e), was summarily dismissed when the court found no causal connection between the allegedly nondisclosed golden parachute contracts[92] and the plaintiff's financial loss. The court's finding stemmed from the refusal by R-H to accept the tendered shares, which caused the plaintiff's injury, prior to the contract negotiations.[93]

Schreiber sharply delineated the tension existing between the common judicial interpretation of Section 14(e) and the actual language of the statute. With the notable exception of *Mobil*, the weight of judicial authority, including *Schreiber*, has construed Section 14(e) solely as a disclosure provision despite the fact that the section specifically prohibits both deceptive and manipulative acts. Any activity in connection with a tender offer that is publicly disclosed, therefore, is not subject to federal securities law under Section 14(e). *Schreiber's* conclusion[94] that deception must be an element of any cause of action under Section 14(e) should prevail in a climate controlled by strict judicial observance of the distinction between state corporate law and federal securities law.

87. *Mobil*, 669 F.2d at 376-77.

88. *Schreiber*, 731 F.2d at 166.

89. "Absent a requirement of deception, the Williams Act would mandate that the federal courts supervise the substantive fairness of practically all tender offers." *Id.*

90. *See supra* note 70.

91. *Schreiber*, 731 F.2d at 166. *See also Santa Fe*, 430 U.S. at 479 (expressing reluctance to federalize state corporate law).

92. *See supra* note 15.

93. *Schreiber*, 731 F.2d at 166.

94. *Id.*

[Casenote by James A. Janda].

TORTS—NEGLIGENCE—SOCIAL HOST WHO SERVES LIQUOR TO A VISIBLY INTOXICATED ADULT GUEST KNOWING THAT GUEST WILL THEREAFTER OPERATE A MOTOR VEHICLE MAY BE HELD LIABLE FOR INJURIES TO THIRD PARTIES CAUSED BY GUEST'S NEGLIGENCE. *Kelly v. Gwinnell*, 96 N.J. 538, 476 A.2d 1219 (1984).

In *Kelly v. Gwinnell*,[1] the Supreme Court of New Jersey held that a social host who serves liquor to a visibly intoxicated adult guest may be held liable for injuries caused by the guest's subsequent drunk driving.[2] The court, basing its decision on common law negligence principles,[3] stated that the crux of the issue was whether a duty should be imposed on social hosts to protect third parties from the foreseeable risks of the host's negligent dispensing of alcohol.[4] In imposing such a duty, the court designated New Jersey as the only state in the nation to allow a pure common law cause of action against social hosts who contribute to the intoxication of their adult guests.[5] The court was careful to point out, however, that the precise scope of the host's duty would have to be developed in future cases.[6]

Donald Gwinnell, a painting contractor, left his home early one evening to assist Joseph Zak, a subcontractor, whose truck was mired in mud. After failing to free the truck, Gwinnell drove Zak

1. 96 N.J. 538, 476 A.2d 1219 (1984).

2. The court narrowly limited its holding to cases in which a host directly serves alcohol to a visibly intoxicated guest knowing that the guest will soon be driving. *Id.* at 546, 476 A.2d at 1228.

3. *Id.* at 543, 476 A.2d at 1221.

4. *Id.* at 544, 476 A.2d at 1222. Although it had been dealt with in lower courts, this was the first time the Supreme Court of New Jersey had addressed the issue. *See* Linn v. Rand, 140 N.J. Super. 212, 356 A.2d 15 (App. Div. 1976) (social host held liable for service of a minor); Figuly v. Knoll, 185 N.J. Super. 477, 449 A.2d 564 (Law Div. 1982) (social host held liable for serving visibly intoxicated adult).

5. *See* Note, *Social Host Liability for Injuries Caused by the Acts of an Intoxicated Guest*, 59 N.D.L. REV. 445, 475 (1983). The supreme courts of California and Oregon have allowed such a cause of action, but their decisions have been legislatively abrogated or limited. *Id.* at 471-73. Other jurisdictions may impose liability for service to persons with certain physical or mental disabilities, but this is an established exception to the old common law doctrine which did not attach liability to those who served alcohol to "ordinary able-bodied men." *See* Cantor v. Anderson, 126 Cal. App. 3d 124, 178 Cal. Rptr. 540 (1981); Comment, *Liquor, the Law, and California: One Step Forward — Two Steps Backward*, 16 SAN DIEGO L. REV. 335, 367-69 (1979) [hereinafter cited as Comment, *Liquor, the Law, and California*]; 45 AM. JUR. 2D *Intoxicating Liquors* §§ 553, 554 (1969); Annot., 97 A.L.R. 3D 528 (1980) (liability based on tort apart from violation of liquor laws); *See also infra* notes 18-82 and accompanying text.

6. 96 N.J. at 556, 476 A.2d at 1228.

home, and then accepted an invitation to come in for a drink. Gwinnell stayed at Zak's house for an hour or two, during which time Gwinnell consumed two or three drinks of scotch.[7] While driving home, Gwinnell collided head on with a vehicle operated by Marie Kelly. Kelly was seriously injured. Based on a blood test taken shortly after the accident, an expert[8] concluded that Gwinnell had been heavily intoxicated at the time of the accident and had been visibly intoxicated while at Zak's residence.[9]

Kelly sued Gwinnell, who filed a third party complaint against Zak and his wife.[10] Kelly then amended her compliant to include the Zaks as direct defendants.[11] The Zaks filed a motion for summary judgment,[12] which the trial court granted. The New Jersey Superior Court, Appellate Division, affirmed.[13] In refusing to allow a cause of action against social hosts for the negligent acts of their intoxicated adult guests the Appellate Division placed itself in accord with the vast majority of jurisdictions that had considered the same question.[14] By doing so, however, the court halted a growing New Jersey trend[15] to expand the liability of one who serves alcoholic beverages.[16] By overturning the Appellate Division, the New Jersey Supreme Court has revitalized the broad liability cases and has taken them one step further.[17]

At common law, the furnishing of intoxicating liquor to an able-bodied man was not a tort.[18] Thus, absent a statute, one injured by

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7. 96 N.J. at 541, 476 A.2d at 1220. It is unclear how much alcohol Gwinnell actually consumed. Zak stated that Gwinnell had two drinks, each containing one shot of liquor. Kelly's expert certified that based on Gwinnell's blood alcohol reading of .286%, he may have had up to 13 drinks. Kelly v. Gwinnell, 190 N.J. Super. 320, 321, 463 A.2d 387, 388 (App. Div. 1983).

8. 96 N.J. at 541, 476 A.2d at 1220.

9. *Id.*

10. *See* N.J. Ct. C.P.R. 4:8-1(a) (defendant is permitted to serve a summons and complaint upon a person who may be liable to him for part of the claim against him).

11. *See id.* at 4:8-1(b) (plaintiff given 20 days after third party complaint to amend his pleading to include the third party defendant).

12. *See id.* at 4:46-2 (to win a summary judgment, movant must show that there is no genuine issue as to any material fact and that he is entitled to judgment as a matter of law).

13. 190 N.J. Super. 320, 463 A.2d 387 (App. Div. 1983).

14. *See* 96 N.J. at 561, 476 A.2d at 1231 (Garibaldi, J., dissenting); Note, *supra* note 6, at 475.

15. In 1959, the Supreme Court of New Jersey handed down the landmark decision of *Rappaport v. Nichols*, the first successful common law negligence action against a tavern owner. *See infra* notes 42-52 and accompanying text.

16. *Id.* at 325-26, 463 A.2d at 390-91. In Linn v. Rand, 140 N.J. Super. 212, 356 A.2d 15 (App. Div. 1976), the Appellate Division allowed a cause of action against social hosts who served minors. *Id. See supra* note 4 and accompanying text.

17. 96 N.J. at 555-56, 476 A.2d at 1228.

18. 45 Am. Jur. 2d *Intoxicating Liquors* § 553 (1969). The rule was qualified in some jurisdictions to allow recovery by third persons against one who sold liquor to one "in such a state of helplessness or debauchery as to be deprived of his willpower or responsibility for his behavior." *Id.* at § 554. For a list of ten jurisdictions which expressly adhere to the common law rule of non-liability, *see* Note, 9 Land & Water L. Rev. 285, 290 n.49 (1984). *See also* McCue v. Klein, 60 Tex. 168 (1883) (liability for inducing drunkard to drink three pints of

an intoxicated actor had no cause of action against the person who supplied the alcohol.[19] The asserted rationale for this rule of nonliability was that no proximate cause[20] existed between the furnishing of the liquor and the subsequent injury.[21] The harshness of this common law rule has been partially mitigated by the passage of dram shop acts,[22] the first of which was adopted in Wisconsin in 1850.[23] Spawned by the temperance movement, dram shop acts sought to discourage the sale of liquor by making tavern keepers strictly liable[24] for any injury to person, property, or means of support caused by the keepers' sale of liquor.[25]

Although dram shop acts provide an alternative to the harshness of the common law rule, they generally have not been extended to cover social hosts.[26] The landmark case rejecting such an expansion is *Cruse v. Aden*.[27] In that case, Julia Ann Cruse sought recovery under the Illinois dram shop act[28] when her husband died after being

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whiskey in rapid succession, causing death); Ibach v. Jackson, 148 Or. 92, 35 P.2d 672 (1934) (getting woman so intoxicated that she fell and was killed).

19. 45 AM. JUR. 2D *Intoxicating Liquors* § 554 (1969). *See, e.g.*, Cole v. Rush, 45 Cal.2d 345, 289 P.2d 450 (1955); Holmes v. Circo, 196 Neb. 496, 244 N.W.2d 65 (1976).

20. 45 AM. JUR. 2D *Intoxicating Liquors* § 553 (1969); Fleckner v. Dionne, 94 Cal. App. 2d 246, 210 P.2d 530 (1949). Dean Prosser has defined proximate cause as "essentially a question of whether the law will extend the responsibility for the conduct to the consequences which have in fact occurred." W. PROSSER, HANDBOOK ON THE LAW OF TORTS § 42 (4th ed. 1971). He further states that "every question which arises in connection with 'proximate cause' [should be stated] in the form of a question: was the defendant under a duty to protect the plaintiff against the event which did in fact occur?" *Id.* For additional discussion of judicial determination of duty and "proximate cause" *see generally* L. GREEN, RATIONALE OF PROXIMATE CAUSE (1927) (discusses the confusion between duty and causation); Bingham, *Some Suggestions Concerning Legal Cause at Common Law* (pts 1 & 2) 9 COLUM. L. REV. 16, 136 (1909) (discussion of the principle of "proximate cause").

21. *Accord* State ex rel Joyce v. Hatfield, 197 Md. 249, 254, 78 A.2d 754, 756 (1951) ("Human beings, drunk or sober, are responsible for their own torts.").

22. Dram shop acts are also referred to as civil damage acts. GRAHAM, *Liability of the Social Host for Injuries Caused by the Negligent Acts of Intoxicated Guests*, 16 WILLIAMETTE L.J. 561, 563 (1980). *See generally* 45 AM. JUR. 2D *Intoxicating Liquors* §§ 561-614 (1969) (elements of cause of action, defenses).

23. Note, *supra* note 5, at 449; 19 LAND & WATER L. REV. 285, 286 n.12 (1984). Other states soon followed suit, and by the turn of the century, most states (including New Jersey) had enacted a dram shop statute. *See* McGough, *Dram Shop Acts*, 1967 A.B.A. SEC. OF INS. NEGL. & COMPENSATION L., 448, 449-50.

24. Strict liability is liability which attaches regardless of any negligence or evil intent. It is based on the idea that defendant has taken action or caused a result which society cannot tolerate. *See* PROSSER, *supra* note 20, at ch. 13.

25. *See generally* 45 AM. JUR. 2D *Intoxicating Liquors* §§ 561-614 (1969).

26. Note, *supra* note 6, at 458. *See, e.g.*, Deloach v. Mayer Elec. Supply Co., 378 So. 2d 733 (Ala. 1979) (required showing of "sale"); Kohler v. Wray, 114 Misc. 2d 856, 452 N.Y.S.2d 831 (Sup. Ct. 1982) (dram shop act applied to "unlawfully contributing to the intoxication," and liquor laws only applied to commercial operations).

27. 127 Ill. 231, 20 N.E. 73 (1889).

28. Dram Shop Act of 1874 (R.S. 1874, p. 438 (current version at ILL. ANN. STAT. Ch. 43, ¶ 135 (West Supp. 1983)). Section 9 of the Act reads, in relevant part, as follows:

> Every husband, wife . . . or other person, who shall be injured in person or property, or means of support by any intoxicated person, or in consequence of the intoxication, habitual or otherwise, of any person, shall have a right of action in his or her own name . . . against any person or persons who shall, by selling

thrown from his horse while intoxicated. Defendant Aden had given Mr. Cruse two drinks which were alleged to have contributed to his intoxication. In rejecting Mrs. Cruse's claim, the Supreme Court of Illinois noted that, because the statute was "of a highly penal nature," it must be strictly construed.[29] This strict construction led the court to hold that the dram shop act only applied to those "engaged in the liquor traffic."[30] In a later case, *Miller v. Owens-Illinois Glass Co.*,[31] the Appellate Court of Illinois warned that extending dram shop liability to social hosts would turn social drinking into a "hazardous act" and "would open up the floodgates of litigation."[32]

Those courts willing to give their state's dram shop acts a broader reach have been promptly overridden by the state legislature. In *Williams v. Klemsrud*,[33] for example, the Iowa Supreme Court found the purpose of its state's dram shop act to be remedial or compensatory in nature, rather than penal.[34] Construing the statute liberally, the court concluded that the dram shop act's grant of a cause of action against "any person" brought the defendant, a non-commercial supplier, within its purview.[35] Shortly after the *Williams* decision, the Iowa Legislature revealed its true intent by repealing the existing dram shop act and enacting a substitute which permitted liability to attach only to commercial purveyors of alcohol.[36] In *Ross v. Ross*,[37] the Minnesota Supreme Court also gave an expansive

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> or giving intoxicating liquors, have caused the intoxication, in whole or in part, of such person or persons . . . .

29. 127 Ill. at 239, 20 N.E. at 77.

30. *Id.* The court reached this decision because most of the act applied exclusively to dram shop owners.

31. 48 Ill. App. 2d 412, 199 N.E.2d 300 (1964) (court refused to hold an employees' association liable under the dram shop act for injuries suffered by plaintiffs in an automobile accident caused by one of the association's intoxicated members after a company picnic).

32. *Id.* at 420, 199 N.E.2d at 306. (The court felt that such an extension should be made by the legislature.); *see also* Miller v. Moran, 96 Ill. App. 3d 596, 421 N.E.2d 1046 (1981) ("whether to provide additional remedies is a legislative rather than a judicial decision").

33. 197 N.W.2d 614 (Iowa 1972). In *Williams*, a twenty-one year-old college student bought liquor for a minor. The minor drank the alcohol, became intoxicated, and was involved in a rear-end collision with plaintiff's vehicle. Plaintiff sought recovery under the state's dram shop act, which read:

> Every . . . person who shall be injured in person or property . . . by any intoxicated person . . . shall have a right of action . . . against any person who shall, by selling or giving to another contrary to the provisions of this title any intoxicating liquors, cause the intoxication of such person, for all damages actually sustained . . . .

IOWA CODE ANN. § 129.2 (West Supp. 1966) (current version at IOWA CODE ANN. § 123.92 (West Supp. 1983)).

34. 197 N.W. 2d at 615-16.

35. *Id.* at 615.

36. Note, *supra* note 6, at 457-58. The statute now allows a cause of action "against any licensee or permittee." IOWA CODE ANN. § 123.92 (West Supp. 1983).

37. 294 Minn. 115, 200 N.W.2d 149 (1972). Defendant bought liquor for his minor brother. After drinking it and becoming intoxicated, the minor drove his car off the road and was killed. Decedent's parents and infant son were awarded damages under Minnesota's dram

reading to its dram shop act,[38] stating that "no reason occurs to us why those who furnish liquor to others, even on social occasions, should not be responsible for protecting innocent third parties from the potential dangers of indiscriminately furnishing such hospitality."[39] Yet, as in *Williams*, this decision was also quickly nullified by legislative action.[40]

Although dram shop acts have never directly provided a cause of action against social hosts, they have contributed to such a cause of action in two ways: first, they utilized the concept of enterprise liability to provide compensation to innocent victims of a socially costly activity;[41] second, they aided the establishment of a common-law cause of action by recognizing the causal link between the furnishing of intoxicating liquor and the injuries caused by an intoxicated recipient of that liquor. Thus, the dram shop acts removed the most formidable barrier to the successful raising of a common law negligence action against a purveyor of intoxicating liquor.[42] Such a cause of action was finally successfully raised in the landmark case of *Rappaport v. Nichols*.[43]

In *Rappaport*, the New Jersey Supreme Court was confronted with the issue of whether to allow recovery against a tavern owner who sold liquor to an intoxicated minor in violation of an alcoholic beverage control statute.[44] The court noted that prior common law claims had been rejected by other courts for proximate cause rea-

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shop act.

38. At the time of the *Ross* case, the dram shop act provided a cause of action "against any person who, by illegally selling, bartering, or *giving* intoxicating liquors . . . ." MINN. STAT. ANN. § 340.95 (West 1972) (emphasis supplied) (current version at MINN. STAT. ANN. § 340.95 (West Supp. 1983)).

39. 294 Minn. at 121-22, 200 N.W.2d at 153 (footnote omitted).

40. Note, *supra* note 6, at 457 n.15. The legislature deleted the word "giving." *See supra* note 37.

41. *See* Comment, *supra* note 6, at 363-64. Enterprise liability is the theory that businesses which market products which cause injury should be held liable for injuries caused by the products because those costs can be distributed among their customers as a cost of doing business. The cost of the injuries will thus be internalized into the price of the product. Comment, *Torts: Liability of the Social Purveyor*, 28 OKLA. L. REV. 204, 206 n.14 (citing Escola v. Coca Cola Bottling Co., 24 Cal. 2d 453, 150 P.2d 436, 441 (1944) (Traynor, J. concurring); *see also* Village of Brooten v. Cudahy Packing Co., 291 F.2d 284, 301 (8th Cir. 1961).

42. *See* Rappaport v. Nichols, 31 N.J. 188, 196, 156 A.2d 1, 5 (1959); *see also* Manning v. Yokas, 389 Pa. 136, 132 A.2d 198 (1957).

43. 31 N.J. 188, 156 A.2d 1 (1959). *Rappaport* was the first case in which civil liability for a third person's injuries was imposed on a tavern owner in the absence of a dram shop act. Note, *supra* note 6 at 401. *See also* Waynick v. Chicago's Last Dep't. Store, 269 F.2d 322 (7th Cir. 1959); Comment, *supra* note 6 at 358 n.19.

44. 31 N.J. at 194, 156 A.2d at 4. Nichols, a minor, was served alcoholic beverages at the defendants' taverns. He became intoxicated, drove his mother's car, and collided with plaintiff's car. Plaintiff's husband was killed in the accident. New Jersey had no dram shop act, but it did have a statute forbidding the sale of alcoholic beverages to minors or visibly intoxicated persons. The Law Division granted the defendants' motion for summary judgment. *See supra* note 12.

sons,[45] but then pointed out that the objection had been weakened by the reasoning of cases decided under dram shop acts.[46] After subjecting the case to a conventional negligence analysis,[47] the court held that the defendant's conduct could readily be found to have been negligent,[48] and that the proximate cause issue was a jury question.[49] In reaching its conclusion, the court relied upon analagous common law negligence cases[50] and weighed relevant policy considerations[51] such as the current problem of drunk driving.[52] Other jurisdictions quickly adopted the holding and reasoning of *Rappaport* by allowing civil liability against liquor vendors who violated alcoholic beverage control laws.[53]

Once a common law cause of action was recognized against tavern owners,[54] it remained to be seen whether the cause of action would be extended to social hosts. The New Jersey Superior Court, Appellate Division, made this extension in *Linn v. Rand*,[55] in which it held that a social host who served intoxicating liquor to a minor could be held liable for injuries to third persons caused by the minor's subsequent negligent acts.[56] Judge Halpern, writing for the

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45. 31 N.J. at 196, 156 A.2d at 5. *See supra* note 20, and authority cited therein.

46. *See supra* note 41.

47. *See* 31 N.J. at 201, 156 A.2d at 8 ("Negligence is tested by whether the reasonably prudent person at the time and place should recognize and foresee an unreasonable risk or likelihood of harm or danger to others.").

48. *Id.* at 202-03, 156 A.2d at 8 (holding that the statute and regulations were for the protection of the general public, the court remarked: "In view of the standard of conduct prescribed by the statute and the regulations, a tavern keeper's sale of alcoholic beverages when he knows or should know that the patron is a minor or is intoxicated may readily be found by the jury to be imprudent conduct."). *See* RESTATEMENT (SECOND) TORTS § 286 (1965) (provides that a penal statute may be adopted as the standard of reasonable conduct if its purpose is to protect the same class of people as the plaintiff and it protects the same interest from the same harm arising from the same hazard).

49. 31 N.J. at 202-03, 156 A.2d at 9. Thus, they could not sustain the granting of the motion for summary judgment. *Id. See also supra* note 12.

50. 31 N.J. at 199-200, 156 A.2d at 7 (citing cases involving negligent entrustment of firearms and cases where violation of a "public safety measure" was held to be evidence of negligence).

51. *Id.* at 205-06, 156 A.2d at 10 (burden to defendant, compensation to innocent victims, strengthening the rule of law).

52. *Id.* at 202, 156 A.2d at 8-9.

53. *See* Vesely v. Sager, 95 Cal. Rptr. 623, 486 P.2d 151 (1971); Prevatt v. McClennan, 201 So. 2d 780 (Fla. Dist. Ct. App. 1967); Elder v. Fisher, 247 Ind. 598, 217 N.E.2d 847 (1966); Pike v. George, 434 S.W.2d 626 (Ky. Ct. App. 1968); Adamian v. Three Sons, Inc., 353 Mass. 498, 233 N.E.2d 18 (1968); Berkely v. Park, 47 Misc. 2d 381, 262 N.Y.S.2d 290 (Sup. Ct. 1965); Mitchell v. Ketner, 54 Tenn. App. 656, 393 S.W.2d 755 (1965).

54. In Soronen v. Olde Milford Inn, Inc., 46 N.J. 582, 218 A.2d 630 (1966), the Supreme Court of New Jersey extended the *Rappaport* rationale to cover service by commercial vendors of intoxicated adults. The court also held that contributory negligence was not a defense to the cause of action. *Id.* at 591, 218 A.2d at 635.

55. 140 N.J. Super. 212, 356 A.2d 15 (App. Div. 1976). In *Linn*, Lucy Rand, a minor, was served alcoholic beverages by Thomas Nacnodovitz while a guest at his home. She became intoxicated and was allowed to drive away. She subsequently ran down and seriously injured plaintiff's infant son. *Id.* Nacnodovitz moved for summary judgment, which was granted by the trial judge. *Id.* at 215, 356 A.2d at 16-17. *See supra* note 12.

56. *Id.* at 220, 356 A.2d at 19. The Appellate Court of California had reached this

court, utilized the same negligence test, that was used in *Rappaport* and recognized the cause of action even though no liquor control statute was at issue.[57] The opinion focused on the inconsistency of allowing social hosts immunity from liability when, under *Rappaport*, commercial vendors were subject to liability for the same culpable conduct.[58] The court further noted the past willingness of New Jersey courts to strike down anomalous tort immunities[59] and impose legal duties where justice demanded. Judge Halpern declared: "[O]ur goal is to do substantial justice in light of our modern day life."[60] Mindful of the serious societal problem created by drunk driving, the court reasoned that imposition of liability was justified.[61]

Although the issue had not reached the New Jersey Supreme Court prior to *Kelly v. Gwinnell*,[62] one New Jersey trial court in *Figuly v. Knoll*,[63] applied the *Linn* holding to impose liability on a social host for serving a visibly intoxicated adult.[64]

Other jurisdictions are divided in their treatment of social host liability.[65] In cases concerning service by a social host of a minor in violation of an alcoholic beverage control statute, the trend appears to be towards imposing liability.[66] Only two jurisdictions, however,

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decision four years earlier in Brockett v. Kitchen Boyd Motor Co., 24 Cal. App. 3d 87, 100 (1972) in which a minor had been served alcohol by his employer in violation of a statute.

57. 140 N.J. Super. at 216-17, 356 A.2d at 18. The court noted that Rand's age had not been established in the record and that the trial judge had granted the summary judgment anyway. *Id.* The court stated the elements of the cause of action as follows:

> [Plaintiff must] prove that (a) Rand was a minor, (b) Nacnodovitz knew she was a minor, knew she intended to drive her car and nevertheless served her alcoholic beverages to the degree that she was unfit to drive, and (c) it was reasonably foreseeable that Rand might injure herself, or others, and that his negligence was a proximate cause of the accident and plaintiff's injuries.

140 N.J. Super. at 217, 356 A.2d at 18.

58. "It makes little sense to say that the licensee in *Rappaport* is under a duty to exercise care, but give immunity to a social host who may be guilty of the same wrongful conduct . . . ." 140 N.J. Super. at 217, 356 A.2d at 18.

59. *Id.* at 218-19, 356 A.2d at 19 (sovereign immunity, charitable immunity, parental immunity, inter-spousal immunity).

60. *Id.* at 218, 356 A.2d at 18-19.

61. *Id.* at 219, 356 A.2d at 19. The court, however, stressed that their holding was strictly limited to the facts of the case, and that they would make future determinations on a case by case basis. *Id.*

62. 96 N.J. 538, 476 A.2d 1219 (1984).

63. 185 N.J. Super. 477, 449 A.2d 564 (N.J. Super. Ct. Law Div. 1982).

64. *Id.* at 580, 449 A.2d at 565. In *Figuly*, Defendant Longfield, a former bartender, served Knoll, whom he characterized as an alcoholic, twelve drinks of vodka and tonic at an afternoon party. Knoll was subsequently involved in a motor vehicle accident in which plaintiff was injured. Longfield moved for a summary judgment. The court denied the motion, asserting that *Rappaport* should be extended to social hosts and that there was nothing in *Linn* to prevent that extension. *Id.*

65. Congini v. Portersville Valve Co., ___ Pa. ___, ___, 470 A.2d 515, 517 (1983).

66. Note, *supra* note 6, at 468; *see* Congini v. Portersville Valve Co., ___ Pa. ___, ___, 470 A.2d 515, 518 (1983) ("an actor's negligence exists in furnishing intoxicants to a class of persons legislatively determined to be incompetent to handle its effects."); *see also* Burke v. Superior Court, 129 Cal. App. 3d 570, 181 Cal. Rptr. 149 (1982); Brattain v. Herron, 159 Ind. App. 663, 309 N.E.2d 150 (1974); Thaut v. Finley, 50 Mich. App. 611, 213 N.W.2d 820 (1973). *But see* Cory v. Schierloh, 174 Cal. Rptr. 500, 629 P.2d 8 (1981); Bald-

have imposed liability on social hosts who furnish intoxicating liquor to visibly intoxicated adult guests, but both of these decisions have been limited by subsequent legislative enactments. In *Wiener v. Gamma Phi Chapter of Alpha Tau Omega Fraternity*,[67] the Supreme Court of Oregon allowed a common law cause of action in negligence to lie against a fraternity which had served alcohol to a minor.[68] The court found that the fraternity had behaved negligently because it knew that the guest was a minor, and realized that he had driven to the party and would have to drive home.[69] The court ruled that the fraternity had a "duty . . . to refuse to serve alcohol to a guest when it would be unreasonable under the circumstances to permit him to drink."[70] The court implied that a similar holding would result when hosts served drinks to visibly intoxicated adult guests[71] but explained that it would not make such a ruling until the facts presented themselves.[72] In 1979, before the case law could develop further, the Oregon legislature passed legislation which limited the *Wiener* holding.[73]

In California, social host liability has put the legislature and the courts somewhat at odds.[74] In *Coulter v. Superior Court*,[75] the Supreme Court of California held that a host who furnished alcohol to a visibly intoxicated adult under circumstances which created a foreseeable risk of harm to others could be liable under a common law negligence theory.[76] The impact of the decision was short lived, how-

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win v. Zoradi, 123 Cal. App. 275, 176 Cal. Rptr. 809 (1981); Keating v. Kroger, 143 Ga. App. 23, 237 S.E.2d 443 (1977).

67. 258 Or. 632, 485 P.2d 18 (1971). In *Wiener*, a college fraternity allowed large quantities of alcohol to be served to a minor guest. The plaintiff, a passenger in the minor's car, was injured when he drove into a building on his way home from the party. *Id.*

68. *Id.* at 638, 485 P.2d at 23.

69. *Id.*

70. *Id.*

71. *Id.* at 636, 485 P.2d at 21 ("Such persons could include those already severely intoxicated . . . .").

72. *Id.*

73. Note, *supra* note 6, at 472. The Oregon Legislature passed OR. REV. STAT. §§ 30.955, .960 (1983). OR. REV. STAT. § 30.955 (1983) provides as follows: "No private host is liable for damages incurred or caused by an intoxicated social guest unless the private host has served or provided alcoholic beverages to a social guest when such guest was visibly intoxicated." OR. REV. STAT. § 30.960 (1983) provides as follows:

> [N]o licensee, permittee, or social host shall be liable to third persons injured by or through persons not having reached 21 years of age who obtained alcoholic beverages from the licensee, permittee or social host unless it is demonstrated that a reasonable person would have determined that identification should have been requested or that the identification exhibited was altered or did not accurately describe the person to whom the alcoholic liquor was sold or served.

74. *See* Note, *supra* note 6, at 468.

75. 21 Cal. 3d 144, 577 P.2d 669 (1978). In *Coulter*, a woman was served large quantities of alcohol by her corporate landlord at a tenant party. She became intoxicated and subsequently drove her car off the road, striking a road abutment and injuring plaintiff, her passenger. *Id.* at 148-49, 577 P.2d at 671.

76. *See supra* note 75.

ever, for just months after it was handed down the California Legislature specifically nullified the result and stipulated that prior case law was top control.[77] The old common law rule that was revived simply states that no cause of action exists for furnishing liquor to an "ordinary man."[78]

Despite the clear legislative intent to limit liability, California courts continued to search for a reason to allow recovery.[79] In *Cantor v. Anderson*,[80] a California appellate court held that liability could be imposed on a social guest who knowingly furnished liquor to a person who, because of an exceptional physical or mental condition, would pose a risk to others if he consumed the liquor.[81] In *Harris v. Trojan Fireworks Co.*,[82] another California appellate court held an employer liable for injuries caused by the drunken driving of an employee returning home from the company Christmas party. Under the peculiar facts of the case, the court found a sufficient nexus between the party and the employer-employee relationship to frame a cause of action under a *respondeat superior* theory.[83] Thus,

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77. CAL. BUS. & PROF. CODE § 25602 (West Supp. 1984) provides as follows:

> (a) Every person who sells, furnishes, gives, or causes to be sold, furnished, or given away, any alcoholic beverage to any habitual or common drunkard or to any obviously intoxicated person is guilty of a misdemeanor.(b) No person . . . [who violates subdivision (a)] shall be civilly liable to any injured person or the estate of such person for injuries inflicted on that person as a result of intoxication by the consumer of such alcoholic beverage.(c) The Legislature hereby declares that this section shall be interpreted so that the holdings in cases such as Vesely v. Sager, Bernhard v. Harrah's Club, and Coulter v. Superior Court be abrogated in favor of prior judicial interpretation finding the consumption of alcoholic beverages as the proximate cause of injuries inflicted upon another by an intoxicated person.

Id. (citations omitted). *But see* CAL. BUS. & PROF. CODE § 25602:1 (West Supp. 1984) ("[A] cause of action may be brought by or on behalf of any person who has suffered injury or death against any person licensed . . . who sells, furnishes, gives or causes to be sold, furnished, or given away any alcoholic beverage to any obviously intoxicated minor . . . .").

78. *See* Cole v. Rush, 45 Cal. 2d 345, 289 P.2d 450 (1955) (states the old common law "consumption rule").

79. Note, *supra* note 6, at 474. *Accord* Blamey v. Brown, 270 N.W.2d 884 (Minn. 1978) *cert. denied* 444 U.S. 1070 (1980) (allowed common law action where dram shop act did not apply to out-of-state supplier); Trail v. Christian, 298 Minn. 101, 213 N.W.2d 618 (1978) (allowed common law action where sale of "3.2 beer" was not covered by dram shop act).

80. 126 Cal. App. 3d 124, 178 Cal. Rptr. 540 (1981). *Cantor* involved a plaintiff who maintained a home for the developmentally disabled. Her neighbor served alcoholic beverages to one of her disabled residents with full knowledge of his disability. The resident became uncontrollably violent and assaulted plaintiff, causing her severe injury.

81. *Id.* at 125, 178 Cal. Rptr. at 542. Defendant relied on Section 25602, *see supra* note 77, claiming that the proximate cause of plaintiff's injury was not the furnishing of the alcohol, but its consumption. *Id.* The court noted that the common law rule was limited to the furnishing of liquor to an *ordinary* man. *Id.* at 130, 178 Cal. Rptr. at 544; *see supra* note 6 (discussing exceptions to the common law rule). Noting that foreseeability is an element of a proximate cause/duty analysis, the court held that if plaintiff could prove that defendant should have foreseen the effect the alcohol would have had on the resident, she would have a cause of action. 126 Cal. App. 3d at 131, 178 Cal. Rptr. at 545; *see also* PROSSER *supra* note 6, § 43, at 257-58 (4th ed. 1971).

82. 120 Cal. App. 3d 157, 174 Cal. Rptr. 452 (1981).

83. *Id.* at 163, 174 Cal. Rptr. at 456. Under *respondeat superior*, an employer is re-

although legislatures have acted to limit liability, courts continue to attempt to impose it where they feel such imposition is just.[84]

Doing "substantial justice"[85] was the prevelant concern of the Supreme Court of New Jersey[86] in *Kelly v. Gwinnell*.[87] The court found the basic elements of a negligence cause of action,[88] but stated that something "more [was] needed;" "more being the value judgment, based on an analysis of public policy, that the actor owed the injured party a duty of reasonable care."[89] In deciding whether to impose that duty, the court focused on two issues: the fairness of imposing liability on social hosts;[90] and the appropriateness of such liability being imposed by the courts instead of the legislature.[91] The court identified policy goals it thought important in resolving this issue, such as the adequate compensation of innocent victims of drunken driving[92] and the reduction of the incidence of drunken driving on New Jersey's highways.[93]

Chief Justice Wilentz, writing for the majority, cited with approval the Appellate Division's holding in *Linn* and reemphasized the concern generated by the inconsistency in immunizing social hosts while imposing liability on licensees.[94] Focusing on the plight of the accident victim, the Chief Justice refused to acknowledge any distinction between social hosts and licensees.[95] The emotionally charged opinion stressed the tremendous social cost of drunk driving and reasoned that the need to provide compensation for its innocent victims outweighed any dislocation in social habits or any threat of disproportionate financial loss to social hosts. While admitting that a social host may be less culpable than an intoxicated adult guest, the

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sponsible for damages due to his servant's want of care if the servant's act occurs in the course of his employment. *See* BLACK'S LAW DICTIONARY 1179 (5th ed. 1979).

84. *See supra* notes 73 and 79 and authority cited therein.

85. *See supra* note 59 and accompanying text.

86. The court was composed of Chief Justice Wilentz and Justices Clifford, Schreiber, Handler, Pollock, O'Hern, and Garibaldi. Chief Justice Wilentz wrote the opinion, and Justice Garibaldi filed a dissenting opinion.

87. 96 N.J. 538, 476 A.2d 1019 (1984).

88. *Id.* at 544, 476 A.2d at 1222 ("the usual elements of a cause of action for negligence are clearly present: an action by defendant creating an unreasonable risk of harm to plaintiff, a risk that was clearly foreseeable, and a risk that resulted in an injury equally foreseeable."). *See generally* PROSSER, *supra* note 6, at § 30 (4th ed. 1971).

89. 96 N.J. at 544, 476 A.2d at 1222.

90. *Id.*

91. *Id.* at 552-53, 476 A.2d at 1226.

92. *Id.* at 551, 476 A.2d at 1226.

93. *Id.* at 544-45, 476 A.2d at 1222.

94. *Id.* at 547, 476 A.2d at 1223-24.

95. *Id.* at 548, 476 A.2d at 1224. *Accord* Coulter v. Superior Court, 21 Cal. 3d at 154, 577 P.2d at 674. ("[I]t is small comfort to the widow whose husband has been killed in an accident involving an intoxicated driver to learn that the driver received his drinks from a hospitable social host rather than by purchase at a bar.) *But cf.* Sites v. Nee, ___ Pa. Super. ___, 477 A.2d 547 (Pa. Super. 1984) ("We do not reach here the question whether liability should be imposed on a defendant who becomes something more than a social host . . .).

Chief Justice stressed that hosts are not faultless,[96] and trial courts could apportion financial responsibility between the host and his guest.[97]

In her well-reasoned dissenting opinion, Justice Garibaldi emphasized the practical differences between social hosts and licensees. The commercial bartender is better qualified to discern intoxication among his customers, and better equipped to deal with dangerously intoxicated people.[98] In contrast, the social host has little expertise in this area, and his disadvantage is compounded by the awkwardness of regulating the alcohol intake of a friend, co-worker, or supervisor. Justice Garibaldi also stressed the superior ability of commercial vendors to spread risks. She noted that while the majority assumed that social hosts could procure liability insurance, it offered no proof that such insurance was readily available or economically feasible.[99] Moreover, the legislature had already provided adequate means of compensation for the victims of accidents caused by drunk drivers.[100]

In a final argument, the dissent asserted that the legislature was the appropriate body to make a public policy decision with such burdensome and far-reaching consequences.[101] Justice Garibaldi argued that the majority had given insufficient consideration to the ramifications of its decision and that, given time, a more creative remedy could be fashioned by the legislature.[102] She also noted the large volume of recent legislative enactments in this area,[103] theorizing that if the legislature had intended to act on the issue of social host liability, it would have done so. Responding to this criticism, the majority interpreted the legislative activity as the enunciation of a policy of

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96. 96 N.J. at 549-50, 476 A.2d at 1225. The Chief Justice drew an analogy to a person who negligently lends his car to an intoxicated person. This is a popular analogy in social host liability cases. *See, e.g.*, Linn v. Rand, 140 N.J. 212, 219, 356 A.2d 15, 19 (App. Div. 1976).

97. *Id* at 548, 476 A.2d at 1224. The Chief Justice also noted that hosts could procure liability insurance. *See also* 9 PEPPERDINE L. REV. 784, 793 (1982) (discussing Ono v. Applegate, 612 P.2d 533 (Hawaii 1980), where the cause of an accident was ruled to be 25% for negligently providing alcohol and 75% for negligent driving).

98. 96 N.J. 565-66, 476 A.2d at 1233-34.

99. *Id.* at 568, 476 A.2d at 1234-35; *But see* Note, *Extension of the Dram Shop Act: New Found Liability of the Social Host*, 49 N.D.L. REV. 67, 81 n. 74 (informal survey showing that increasing coverage of homeowner's or renter's policy would be inexpensive).

100. 96 N.J. 564, 476 A.2d at 1232-33. Payment would initially be expected to come from the drunk driver's insurance. If he was uninsured, payment would come from the individual's own policy which is required by law to include uninsured motorist coverage, *see* N.J. STAT. ANN. § 39:6A-14 (West 1973). If the victim was a pedestrian and could not recover from the driver's insurance, they could recover from the Unsatisfied Claims and Judgments Fund, *see* N.J. STAT. ANN. § 39:6-72. The only time that there might be no recovery is when the victim himself is illegally driving without insurance.

101. 96 N.J. at 560, 476 A.2d at 1230.

102. *Id.* at 569, 476 A.2d at 1235.

103. *Id. See, e.g.*, 1983 N.J. SESS. LAW 574 (West) (imposing fine and one year loss of driver's license for minor attempting to buy liquor and for anyone supplying minor with false identification); *Id.* at 39 (four month mandatory minimum sentence for conviction of "death by auto" while driving under the influence).

deterrence of drunk driving, concluding that the court's decision would further that policy.[104] The majority noted that determination of the scope of duty in negligence cases was a proper judicial function, and that if the legislature disagreed with the court's decision, it could take remedial action.[105]

The New Jersey Legislature has initiated such remedial action with the recent introduction of Assembly Bill 43.[106] Thus, it appears that the *Kelly* case will soon join *Williams*, *Ross*, and *Coulter* in the ranks of legislatively abrogated case law.[107] Although courts normally impose duties in tort cases, the imposition of a duty whose discharge is so onerous is more properly the function of an innovative and representative legislature. Although a primary goal of tort law is to provide compensation for innocent victims,[108] obtaining such compensation from social hosts would require that such hosts be subjected to a standard which would approach strict liability in the hands of a jury — a result both unnecessary and unjust. It is unnecessary because of the legislature's capacity to fashion alternate means of providing adequate compensation for victims. It is unjust because of the limited control a social host has over his guests' consumption of alcohol and their subsequent actions. Most likely, decisions like *Kelly* which arise in the future will also suffer legislative abrogation. And it seems equally likely that legislative action in this area will remain vigorous.

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104. 96 N.J. at 544-45, 476 A.2d at 1222.
105. *Id.* at 555, 476 A.2d at 1227.
106. A. 43, 201st. Leg., 1st Sess. (1984). The bill reads in relevant part, as follows:
> No person, other than a person licensed . . . to sell alcoholic beverages, who furnishes any alcoholic beverages, to a person at or over the age at which a person is authorized to purchase and consume alcoholic beverages shall be civilly liable to any person or the estate of any person for personal injuries or property damage inflicted as a result of intoxication by the consumer of the alcoholic beverages.

107. *See supra* notes 32-39, 72-78 and accompanying text.
108. *See* PROSSER *supra* note 6, at § 1 (functions of tort law).

[Casenote by Stephen R. Thelin].

CONTRACTS — INSURANCE LAW — CLEARLY WORDED AND CONSPICUOUSLY DISPLAYED EXCLUSIONS IN AN INSURANCE CONTRACT CANNOT BE AVOIDED DESPITE INSURED'S LACK OF KNOWLEDGE OR UNDERSTANDING. *Standard Venetian Blind Co. v. American Empire Insurance Co.*, 503 Pa. 300, 469 A.2d 563 (1983).

In *Standard Venetian Blind Co. v. American Empire Insurance Co.*,[1] a divided[2] Pennsylvania Supreme Court held that clearly worded and conspicuously displayed[3] exclusion clauses in an insurance contract cannot be avoided by an insured who lacks knowledge or understanding of the exclusion clauses. The court explicitly rejected the interpretive standard that had been applied in a line of Pennsylvania cases since 1974, which enforced the exclusions only after the insurer proved that the exclusions and their effect had been explained to the insured.[4] The majority also declined to adopt the "reasonable expectations" standard[5] used in other jurisdictions. Rather, the court's opinion evinced that traditional contract principles should be employed to determine the parties' rights and obligations under an insurance contract.

A complaint filed against the Standard Venetian Blind Company precipitated[6] the company's controversy with its insurer. The complaint, filed by D.H. Evans, alleged that Standard Venetian Blind, a general contractor, breached express and implied warranties[7] under a construction contract. The contract provided that a subcontractor of Standard Venetian Blind would install a portico on Evans' property. The portico was completed in 1974, but four years later a heavy snowstorm caused it to collapse. The portico was de-

1. 503 Pa. 300, 469 A.2d 563 (1983).

2. Chief Justice (now Justice) Roberts delivered the opinion of the court, and was joined by Justices Larsen, McDermott, and Zappala. Justice Hutchinson wrote a concurring opinion in which Justice Flaherty joined. Justice (now Chief Justice) Nix wrote a brief dissent.

3. *See infra* notes 73-76 and accompanying text.

4. *See infra* notes 55-64 and accompanying text.

5. *See infra* notes 42-51 and accompanying text.

6. In Pennsylvania, an insurer's duty to defend coverage afforded by a policy arises when a complaint filed against the insured alleges liability that would potentially be covered under the insurance policy. Gedeon v. State Farm Mut. Auto. Ins. Co., 410 Pa. 55, 188 A.2d 320 (1963).

7. Evans alleged that Standard Venetian Blind warranted that the portico "would not collapse under weights of snow or ice far beyond those seen in the Wilkes-Barre area." 503 Pa. at 310, 469 A.2d at 568 (Hutchinson, J., concurring).

molished and Evans incurred, in addition to the cost of replacing the portico, the consequential expenses of repairing property stored beneath the portico and clearing away the debris.[8]

Standard Venetian Blind was insured by the American Empire Insurance Company under a comprehensive general liability policy[9] issued in 1975. The policy provided personal injury and property damage coverage, committing the insurer to indemnify the insured for those sums for which the policyholder became legally obligated, and requiring the insurer to defend property damage. American Empire Insurance conceded coverage for the consequential damages assumed by Evans, however, the insurer refused to defend or to indemnify Standard Venetian Blind in connection with Evans' claim for the sum of money needed to replace the portico itself.[10] The denial of coverage was based on two provisions[11] included in a list of exclusions that followed the coverage section of the policy.

While the breach of warranty claim filed by Evans was awaiting trial,[12] Standard Venetian Blind initiated a declaratory judgment action[13] seeking a determination that its liability to Evans was covered by the policy. Depositions and testimony emanating from the declaratory judgment action revealed that the insurance contract had been executed by Sheldon B. Morris, one of Standard Venetian Blind's partners, and Boris H. Levitsky, an employee of Block Brothers Insurance Company acting as agent for American Empire Insurance. Morris asserted that he relied on Block Brothers Insurance to pro-

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8. 503 Pa. at 302, 469 A.2d at 565.

9. 503 Pa. at 310, 469 A.2d at 568 (Hutchinson, J., concurring).

Insurance policies are normally standardized policies generated by industry trade groups. *See infra* note 35. For a reproduction of the 1966 version of the Comprehensive General Liability Policy prepared by the National Bureau of Casualty Underwriters, see Elliott, *The New Comprehensive General Liability Policy* in LIABILITY INSURANCE DISPUTES 12-1, 12-33 to 12-36 (S. Schreiber ed. 1968). This version was slightly modified in 1973. *See* 2 R. LONG, THE LAW OF LIABILITY INSURANCE § 11.01 (1979).

10. 503 Pa. at 304, 469 A.2d at 565.

11. The following provisions formed the basis for denying coverage:

> This insurance does not apply: . . .
>
> (n) to property damage to the named insured's products arising out of such products;
>
> (o) to property damage to work performed by or on behalf of the named insured arising out of the work or any portion thereof or out of materials, parts or equipment furnished in connection therewith.

The policy defined the phrase "named insured's products" as "goods or products manufactured, sold, handled, or distributed by the named insured or others trading under his name. . . ." *Id.* at 303, 469 A.2d at 565 (quoting from the policy).

12. The outcome of Evans' suit was a jury verdict against Standard Venetian Blind in the amount of $13,094.64, which reflected compensation for replacing the portico and for Evans' consequential damages. 503 Pa. at 309, 469 A.2d at 568 (Hutchinson, J., concurring). The judgment entered by the trial court was affirmed in Evans v. Standard Venetian Blind Co., 295 Pa. Super. 576, 435 A.2d 926 (1981).

13. Declaratory judgments are permitted in Pennsylvania under 42 PA. CONS. STAT. ANN. §§ 7531-41 (Purdon 1982).

vide "full coverage for everything we have,"[14] which included "fire insurance, our products liability, our contingent liability and all of the items that go into making up these policies."[15] Morris testified that he had received the policy, but that he had filed it away without ever reading it.[16]

The trial court found that the policy exclusions were "plain and free of ambiguity"[17] and, if enforced, would exclude from coverage the insured's liability for the damage to the portico itself. Nevertheless, the court, relying on a line of cases following the 1974 Superior Court decision of *Hionis v. Northern Mutual Insurance Co.*,[18] refused to apply the exclusions since American Empire Insurance was unable to prove that the insured had an awareness and understanding of the exclusions. The Superior Court affirmed, also applying the *Hionis* standard. On appeal, the Pennsylvania Supreme Court interpreted the policy using traditional contract law, reversed the Superior Court, and directed that judgment be entered for the insurer.[19]

Contract law, the standards around which individuals are able to legislate the rules governing their relationships,[20] emerged in its classical form following the Industrial Revolution and the development of market economies.[21] Fundamental to the new law was the premise that a contract is a private transaction between individuals who meet by chance in the marketplace and bargain on equal footing.[22] As a result, the government was expected to — and did — refrain from restraining or interfering[23] in contractual relationships. The courts, however, were called on to interpret and to enforce these

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14. 503 Pa. at 304, 469 A.2d at 565 (quoting from the trial record).

15. 503 Pa. at 312, 469 A.2d at 570 (Hutchinson, J., concurring) (quoting from the trial record).

16. 503 Pa. at 303, 469 A.2d 565.

17. *Id.*

18. 230 Pa. Super. 511, 327 A.2d 363 (1974); *see also infra* notes 55-64 and accompanying text.

19. 503 Pa. at 307, 469 A.2d at 567.

20. *See generally* Slawson, *Standard Form Contracts and Democratic Control of Lawmaking Power*, 84 HARV. L. REV. 529 (1971).

21. Kessler, *Contracts of Adhesion — Some Thoughts About Freedom of Contract*, 43 COLUM. L. REV. 629 (1943).

In Holmes, *A Contextual Study of Commercial Good Faith: Good Faith Disclosure in Contract Formation*, 39 U. PITT. L. REV. 381 (1978), the author pinpoints the beginning of the scientific formality of contract law at 1871, the year in which Langdell published the first casebook on contracts. The fundamental principles embodied in this casebook were followed by the works of Holmes and Williston, which further developed the pure doctrine while viewing narrowly the social duties of the parties. *But see* Horwitz, *The Historical Foundations of Modern Contract Law*, 87 HARV. L. REV. 917 (1974); Horwitz, Book Review, 42 U. CHI. L. REV. 787 (1975) (reviewing G. GILMORE, THE DEATH OF CONTRACT (1974)).

22. Farnsworth, *The Past of Promise: An Historical Introduction to Contract*, 69 COLUM. L. REV. 576 (1969); Kessler, *supra* note 21 at 630.

23. The high water mark for freedom of contract proponents may have been reached during the era of Lochner v. New York, 198 U.S. 45 (1905), Adair v. United States, 208 U.S. 161 (1908), and Coppage v. Kansas, 236 U.S. 1 (1915). These decisions elevated freedom of contract to a property right constitutionally protected from governmental interference.

agreements. The necessity for predictability of rights and obligations in the new economy led to the evolution of scientific-legal principles[24] that focused on defects in contract formation,[25] which tended to simplify the interpretive process. Three examples of these judicially-contrived rules are: the *contra proferentem* rule, a rule designed to resolve ambiguities in language,[26] the doctrine that clear and unambiguous language does not give rise to an "opportunity for interpretation or construction,"[27] and the principle that a party has a duty to read a contract before assenting to it.[28]

The disparities between an insurance contract and a contract formed in the manner contemplated by the *laissez fiare* capitalists have long been acknowledged.[29] The primary difference[30] is that an

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24. The development of discrete rules may have been more than a practical necessity. The Classical Individualism philosophy, which was most influential between 1850 and 1940, has been reduced to three basic propositions:

> [1.] [T]here should exist an area of individual autonomy within which there is no responsibility at all for effects on others. . . . [2] [T]here are only two legitimate sources of liability: fault . . . and contract. . . . [3] [T]he concepts of fault and free will to contract can *generate*, through a process of deduction, *determinate legal rules defining the boundaries and content of tort and contract duties.*

Kennedy, *Form and Substance in Private Adjudication*, 89 HARV. L. REV. 1685, 1728-29 (1976) (footnotes omitted) (emphasis added).

25. Comment, *Unconscionability in Standard Form*, 64 CALIF. L. REV. 1151 (1976).

26. The following is a restatement of the *contra proferentem* rule: "Since one who speaks or writes, can by exactness of expression more easily prevent mistakes in meaning, than the one with whom he is dealing, doubts *arising from ambiguity* of language are resolved in favor of the latter." 4 S. WILLISTON, A TREATISE ON THE LAW OF CONTRACT § 621, at 760-61 (3d ed. 1961) (footnotes omitted) (emphasis added). Since the rule deals with ambiguity existing at the time of assent, it addresses a defect in formation.

In an insurance context, the rule has been stated as "the familiar principle that insurance policies be strictly construed against the insurer, and that ambiguities and doubts and equivocal words be construed against the insurer and be resolved in the insured's favor." Mohan v. Union Fidelity Life Ins. Co., 207 Pa. Super. 205, 216 A.2d 342, 347 (1966), *aff'g per curiam* 38 Pa. D. & C.2d 401, 410 (1965).

Pennsylvania cases applying the rule early this century include MacDonald v. Metropolitan Life Ins. Co., 304 Pa. 213, 155 A. 491 (1931); Brams v. New York Life Ins. Co., 299 Pa. 11, 148 A. 855 (1930); Francis v. Prudential Ins. Co., 243 Pa. 380, 90 A. 205 (1914).

The meaning of the term "ambiguity" is clearly consequential. *See infra* note 73.

27. 4 S. WILLISTON, *supra* note 26, § 609, at 402.

28. Johnson v. Patterson, 114 Pa. 398, 6 A. 746 (1886); *see also* 1 S. WILLISTON, *supra* note 26, § 35.

For an analysis of the competing policy considerations which circumscribe the bounds of the duty to read, and application of the analysis to the unauthorized use of a credit card, see Macaulay, *Private Legislation and the Duty to Read — Business Run by IBM Machine, the Law of Contracts and Credit Cards*, 19 VAND. L. REV. 1051 (1966).

29. Consider this excerpt from an 1878 opinion:

> Insurance contracts are prepared by insurers who have at their command in their preparation the best legal talent and business capacity, and every precaution is taken for their protection. This is made necessary to prevent the frauds of bad men. But on the other hand the insured are generally plain men without counsel, or the capacity to understand the involved and complicated writings which they are required to sign, and which in most cases probably they never read. What they understand is that they are to pay the insurers so much money, and if they are burnt out the insurers pay them so much.

Willis v. Germania & Hanover Fire Ins. Cos., 79 N.C. 218, 220-21 (1878).

30. Holmes notes two other unique qualities of insurance contracts. First, an insured's

insurance contract is a contract of adhesion,[31] as a result of the way it is prepared and marketed. Unlike an ordinary contract, the insurance contract is formed by parties whose relative bargaining power and knowledge are disproportionate,[32] written in language that is extraordinarily technical from the insured's point of view,[33] often delivered to the insured as a completed policy only after contract formation,[34] and standardized, so that the insured has little choice of terms or language.[35] The need for control resulting from abuses by insurers[36] led to the development of "rights against insurers at variance with policy provisions."[37] These controls comprised legislative[38] action and judicial interpretation that favored the insured. Despite this preference for the insured, early twentieth century courts were reluctant to openly admit that their decisions were at variance with the policy language, preferring to cast their decisions within the discrete rules of classical contract theory.[39] For example, in order to apply

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potential economic harm is greater than that of a party to a general contract. In the event of an unexpiated breach, the insured's fortuitous loss is compounded by his loss of expectation (coverage) and premiums, but a party to an ordinary contract would expect to lose at most his expectation interest. Second, four competing interests (those of the insured, the insurer, other policyholders, and the public in general) must be considered, as compared with the two interests treated by the classical contract theorists. Holmes, *supra* note 21, at 396.

31. The term "contract of adhesion" referring to an agreement in which one party has little choice of terms, was coined in Patterson, *The Delivery of a Life-Insurance Policy*, 33 HARV. L. REV. 198, 222 (1919).

32. Holmes, *supra* note 21, at 397; Kessler, *supra* note 21, at 632.

33. Holmes, *supra* note 21, at 397; Standard Venetian Blind Co. v. American Empire Ins. Co., 503 Pa. 300, 313, 469 A.2d 563, 570 (Hutchinson, J., concurring) ("Such policies are ordinarily 'clear' and 'unambiguous,' if at all, only to underwriters, statisticians or actuaries who have expert knowledge in the evaluation and classification of risks.").

Herbert Denenberg, Pennsylvania's former consumer-minded Insurance Commissioner, applied readability tests to insurance contracts and other writings. On a scale ranging to 100, with 100 corresponding to perfect readability, Denenberg reported the following scores: Joe Garagiola's book, "Baseball is a Funny Game," scored an 80, a revised edition of the Bible was rated at 67, a version of Einstein's Theory of Relativity achieved 18, and various insurance contracts ranged between ten and minus two. O'Connell, *Living with Life Insurance*, N.Y. Times, May 19, 1974, § 6 (Magazine), at 34 (also cited at Holmes, *supra* note 21, at 397 n.67).

34. Holmes, *supra* note 21, at 397; Slawson, *supra* note 20, at 545.

35. Insurance policies are standardized intercompany as well as intracompany. Standardized insurance policy provisions are periodically adopted by the National Bureau of Casualty Underwriters for use by the insurance companies that comprise its membership. Nonmember insurers often use the same policy provisions. Elliott, *supra* note 9, at 12-3.

Standardization should not be viewed as completely contrary to the interests of the policyholder and the public. Since they facilitate accurate bulk calculation of risk by pooling the experience of many companies, standardized contracts promote predictability and add efficiency to the insuring process. The insurance companies' efficiency is transferred to the consumer as lower premiums. R. KEETON, BASIC TEXT ON INSURANCE LAW § 2.10 (1971).

36. R. KEETON, *supra* note 35, § 6.2.

37. *Id.* at 348.

38. *See, e.g.*, PA. STAT. ANN. tit. 40, § 477b (Purdon Supp. 1984-1985), which provides that policy provisions must be approved by the Insurance Commissioner in order for the provisions to be lawfully used in Pennsylvania. Unapproved language in a policy would not be given effect.

39. Holmes, *supra* note 21, at 398.

[C]ourts have made great efforts to protect the weaker contracting party and

the *contra proferentem* rule,[40] judges strained to find ambiguity in apparently straightforward provisions of insurance contracts.[41]

Courts began to accept more openly a "legal realism"[42] approach to the interpretation of insurance contracts in the early 1960's.[43] Rather than employing traditional contract interpretive techniques, some courts applied new and unique doctrines and principles.[44] Professor Keeton described the most important and influential of these doctrines: "The objectively reasonable expectations of applicants and intended beneficiaries regarding the terms of insurance contracts will be honored even though painstaking study of the policy provisions would have negated those expectations."[45] This doctrine of reasonable expectations has been accepted[46] in its purest form[47] only in Alaska[48] and New Jersey.[49] Courts in other states have used the doctrine, but only after finding an ambiguity in the

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> still keep "the elementary rules" of the law of contracts intact. As a result, our common law of standardized contracts is highly contradictory and confusing, and the potentialities inherent in the common law system for coping with contracts of adhesion have not been fully developed.

Kessler, *supra* note 21, at 633.

40. *See supra* note 26.

41. Kessler, *supra* note 21, at 633; Keeton, *Reasonable Expectations in the Second Decade*, 12 FORUM 275, 278 (1976). *See also* cases cited *infra* note 54.

42. *See generally* Kennedy, *supra* note 24.

43. Keeton, *supra* note 41.

Keeton credits the following passage from Kievit v. Loyal Protective Life Ins. Co., 34 N.J. 475, 482, 170 A.2d 22, 26 (1961), as foreshadowing a basic change in insurance law: "When members of the public purchase policies of insurance they are entitled to the broad measure of protection necessary to fulfill their reasonable expectations." Keeton, *supra* note 41, at 275.

44. An example of one such approach is the "Wayfaring Fool" doctrine. Young, Lewis & Lee, *Insurance Contract Interpretation: Issues and Trends*, 1975 INS. L.J. 71, 74 (duty of insurer to use language sufficiently clear that a "wayfaring man, though a fool, might not be deceived"). *See also* Leff, *Contract as Thing*, 19 AM. U.L. REV. 131 (1970) (advocating that a contract be viewed as a thing with the result that warranty theories would apply).

45. Keeton, *Insurance Law Rights at Variance with Policy Provisions* (pt. 1), 83 HARV. L. REV. 961, 967 (1970). At the time it was put forth, Keeton termed reasonable expectations a "principle," i.e., a method of *explaining* the inconsistent judicial opinions in insurance contract interpretation.

46. The reasonable expectations doctrine has not been without its critics, as the following passage suggests: " 'Reasonable expectations' is a euphemism for 'reasonable deal.' Thus, courts have decided that it is permissible to rewrite the terms of insurance contracts where they feel a 'raw deal' has resulted. Contract law has, in this context, at least, become 'contort law.' " Haley, *The Interpretation of Ambiguous Terms of Bankers Blanket Bonds* (pt. 1), 18 FOR THE DEFENSE 29, 31 (1977).

Additionally, courts have rejected the reasonable expectations approach. *See* Casey v. Highlands Ins. Co., 100 Idaho 505, 600 P.2d 1387 (1979) (rejecting the insured's assertion that an earlier plurality opinion embraced reasonable expectations); Morgan v. State Farm Life Ins. Co., 240 Or. 113, 400 P.2d 223 (1965).

47. The purest form of the doctrine would honor a policyholder's reasonable expectations even "when the language of an unusual provision is clearly understandable." Keeton, *supra* note 45, at 968.

48. INA Life Ins. Co. v. Brundin, 533 P.2d 236 (Alaska 1975); Continental Ins. Co. v. Bussell, 498 P.2d 706 (Alaska 1972).

49. DiOrio v. New Jersey Mfr. Ins. Co., 79 N.J. 257, 398 A.2d 1274 (1979); Bryan Constr. Co. v. Employers' Surplus Lines Ins. Co., 60 N.J. 375, 290 A.2d 138 (1972); Jones v. Continental Casualty Co., 123 N.J. Super. 353, 303 A.2d 91 (1973).

policy provisions.[50] So many judicial opinions had paid homage to the approach, that by 1976 Professor Keeton termed the acceptance of reasonable expectations as "explicit judicial endorsement of a new ground of decision — a development connoted by the term 'doctrine.' "[51]

During the 1960's and early 1970's, Pennsylvania courts were reluctant to relinquish well-settled contract law principles in favor of the new reasonable expectations technique of contract interpretation. The judiciary readily applied the language of the insurance contract against the interests of the insured when the insured was a business organization.[52] When the policyholder was an individual consumer, however, the courts strained to find an ambiguity in order to create an opportunity to apply the *contra proferentem*[53] rule against the insurance company.[54]

The 1974 Superior Court case, *Hionis v. Northern Mutual Insurance Co.*,[55] commenced a new phase in insurance contract interpretation in Pennsylvania. In ruling on whether a provision in a fire insurance policy covering the policyholder's improvements to rented property[56] could be used to reduce the full policy benefits, the court

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50. *See* cases from California, Connecticut, Georgia, Maryland, Michigan, Minnesota, New Mexico, New York, North Carolina, North Dakota, Texas, and Washington cited at Comment, *A Reasonable Approach to the Doctrine of Reasonable Expectations as Applied to Insurance Contracts*, 13 U. MICH. J.L. REF. 603, 609 n.22 (1980).

51. Keeton, *supra* note 41, at 276.

52. Eastcoast Equip. v. Maryland Casualty Co., 207 Pa. Super. 383, 218 A.2d 91 (1966).

53. *See supra* note 26.

54. *See, e.g.*, Frisch v. State Farm Fire and Casualty Co., 218 Pa. Super. 211, 275 A.2d 849 (1971). In *Frisch*, the defendant insurer issued a homeowners policy which excluded from coverage injuries to persons on the insured's premises "because of a business conducted thereon." *Id.* at 213, 275 A.2d at 850. The plaintiff was injured when he fell from a ladder while painting the policyholder's house. The court held that an ambiguity existed in the policy because the exclusion did not distinguish between persons who are on the premises while patronizing a business operated by the property owner and persons who are conducting business on the premises as business invitees of the owner. Therefore, the court found that coverage did exist and reversed the trial court's judgment for the insurer. *See also* Purdy v. Commercial Union Ins. Co., 50 Pa. D. & C.2d 230 (1970) (Allegheny Co. Court of Common Pleas).

For other opinions utilizing varying degrees of ambiguity to support a ruling in favor of the policyholder, see Papadell v. Harleysville Mut. Casualty Co., 411 Pa. 214, 191 A.2d 274 (1963); Evans v. Baltimore Life Ins. Co., 216 Pa. Super. 425, 268 A.2d 155 (1970); Barth v. State Farm Fire and Casualty Co., 214 Pa. Super. 434, 257 A.2d 671 (1969).

55. 230 Pa. Super. 511, 327 A.2d 363 (1974) (Hoffman, J.).

56. The provision relied on by the insurance company stated:

> (3) [T]he liability of this company should be determined as follows:
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> . . .
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> (b) If not repaired or replaced within a reasonable time after such loss, that portion of the original cost at the time of installation of the damaged or destroyed improvements and betterments, which the unexpired term of the lease at the time of the loss bears to the period(s) from the date(s) of such improvements and betterments were made to the expiration date of the lease.

Id. at 514, 327 A.2d at 364 (emphasis deleted). Since the insured did not replace the improvements promptly because of the unavailability of financing, the insurer offered him $12,733.86 as the value of the remaining use interest of the improvements which had been insured for $49,500.

stated in dictum,[57] "Even where [sic] a policy is written in unambiguous terms, the burden of establishing the applicability of an exclusion or limitation involves proof that the insured was aware of the exclusion or limitation and that the effect thereof was explained to him."[58] Later court opinions[59] readily employed this language, which clearly went beyond the ostensibly objective[60] reasonable expectations approach by hinging the coverage question on the subjective mental state of the policyholder. Hailed as a standard by which the adhesive nature of an insurance contract can be counterbalanced,[61] the *Hionis* standard was widely accepted as law in Pennsylvania.[62] The standard created practical problems for insurance companies, however, since it decreased[63] the predictability of the legal effect of an insurance policy and potentially reduced the coverage dispute to weighing the credibility of the policyholder against that of the insurer's agent.[64]

The Pennsylvania Supreme Court had its first opportunity to endorse or reject the *Hionis* approach in *Standard Venetian Blind Co. v. American Empire Insurance Co.*[65] The court's decision, which has been[66] and will be relied upon to frame the degree of control that lower courts are to exercise over insurance contracts, instructed that traditional principles of contract law interpretation[67] rather than

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57. The passage was termed "dictum" by the concurring justices in *Standard Venetian Blind*, 503 Pa. at 313, 469 A.2d at 570 (Hutchinson, J., concurring), presumably because the *Hionis* court termed the policy language "technical and unclear," 230 Pa. Super. at 517, 327 A.2d at 366, requiring only an application of the *contra proferentem* rule.

58. 230 Pa. Super. at 517, 327 A.2d at 365 (emphasis added).

59. Selected Risks Ins. Co. v. Bruno, 718 F.2d 67 (3d Cir. 1983); O'Malley v. Continental Ins. Co., 305 Pa. Super. 302, 451 A.2d 542 (1982); Kelmo Enters. v. Commercial Union Ins. Co., 285 Pa. Super. 13, 426 A.2d 680 (1981); Oliver B. Cannon & Son, Inc. v. Fidelity & Casualty Co., 484 F. Supp. 1375 (D.Del. 1980) (applying Pennsylvania law); Klischer v. Nationwide Life Ins. Co., 281 Pa. Super. 292, 422 A.2d 175 (1980); *cf.* Brokers Title Co. v. St. Paul Fire & Marine Ins. Co., 610 F.2d 1174 (3d Cir. 1979).

60. W. Keeton, *supra* note 45, at 967-68. *But see* Comment, *A Reasonable Approach to the Doctrine of Reasonable Expectations as Applied to Insurance Contracts*, *supra* note 50, at 617-18 (lack of guidelines for determining reasonableness renders reasonable expectations doctrine subjective).

61. *See, e.g.*, Standard Venetian Blind Co. v. American Empire Ins. Co., 503 Pa. 300, 321, 469 A.2d 563, 574 (1983) (Nix, J., dissenting).

62. Bishop v. Washington, No. 83-1818, slip op. at 6-7 (Pa. Super. July 6, 1984); *see also* cases cited in note 60 *supra*.

63. Standard Venetian Blind Co. v. American Empire Ins. Co., 503 Pa. 300, 306, 469 A.2d 563, 567 (1983).

64. *Id.*

65. 503 Pa. 300, 469 A.2d 563 (1983).

66. The following cases have been decided by relying on the *Standard Venetian Blind* decision, and have been resolved in favor of the insurer: Bishop v. Washington, No. 83-1818, slip op. (Pa. Super. July 6, 1984); Patula v. Northwestern Nat'l Ins. Co., No. 84-27056, slip op. (Pa. Super. July 6, 1984); Haegele v. Pennsylvania Gen. Ins. Co., No. 83-1663, slip op. (Pa. Super. June 22, 1984); Votedian v. General Accident Fire and Life Assurance Corp., No. 83-2399, slip op. (Pa. Super. June 8, 1984).

67. The court began its analysis with a recitation of the principles that were to govern:

> The task of interpreting a contract is generally performed by a court rather than by a jury. . . . The goal of that task is, of course, to ascertain the intent of the

those of *Hionis* should be used. The court refused to deviate from the "clear and unambiguous"[68] language of the policy exclusions since to do so "would require [the court] to rewrite the parties' written contract."[69] That the policyholder was not apprised of the effect of the exclusions, did not read the contract, and may have reasonably expected coverage, afforded him no relief from the provisions. The majority gave the exclusions their full effect and decided that Standard Venetian Blind's claim was properly denied by American Empire Insurance.

The court supported the use of traditional contract law with the assertion that desirable policy goals of keeping insurance costs low and facilitating rapid resolution to coverage questions would thereby be enhanced.[70] By placing greater weight on the language of the policy, the court reasoned that the insurer attains greater confidence in the policy which allows him to reduce the judicial risk[71] component of premiums. Additionally, the greater certainty discourages litigation and the associated costs and delays. The majority opinion impliedly criticized *Hionis* for boosting insurance costs and contributing to delays, and consequently ordered: "*Hionis* . . . is not to be followed."[72]

Strict enforcement of the language of the contract's limiting provisions by the application of the *Standard Venetian Blind* approach presupposes a finding that the provisions are unambiguous.[73]

> parties as manifested by the language of the written instrument. . . . Where a provision of a policy is ambiguous, the policy provision is to be construed in favor of the insured and against the insurer, the drafter of the agreement. . . . Where, however, the language of the contract is clear and unambiguous, a court is required to give effect to that language. . . . "[I]n the absence of fraud, 'failure to read [the contract] is an unavailing excuse or defense and cannot justify an avoidance, modification or nullification of the contract or any provision thereof.' "

503 Pa. at 304-05, 469 A.2d at 566 (citations omitted). Courts traditionally used these principles to interpret contracts. *See supra* notes 26-28 and accompanying text.

68. 503 Pa. at 306, 469 A.2d at 566.

69. *Id.*

70. *Id.* at 306, 469 A.2d at 567.

71. "Judicial risk" refers to the risk carried by the insurance company that a court will decide a coverage question adversely even though the insurer did not intend the policy to cover the contingency and therefore did not otherwise base its premium on the risk that that contingency would occur.

72. 503 Pa. at 306, 469 A.2d at 567.

73. Whether the traditional contract law approach, which shifts the focus of inquiry from the existence of the policyholder's understanding or reasonable expectations to the existence of an ambiguity, furthers the desire for objectivity has been questioned. "The greatest hindrance to predictability in standard insurance contract analysis is the use of the term 'ambiguity.' " Comment, *A Reasonable Approach to Reasonable Expectations as Applied to Insurance Contracts*, *supra* note 50, at 606. The author has identified three sources of ambiguity: first, the inconspicuousness of exclusionary clauses which fail to adequately warn the policyholder of a limitation on coverage; second, terms which are incorrect, uncertain or unclear resulting in ambiguity because the scope of coverage is uncertain or a definition is unclear or illogical; and third, extrinsic information, such as brochures or applications, which may not be consistent with the policy. *Id.* at 606-07.

Since provisions that can be termed "ambiguous" would be open to more liberal treatment, the key question in terms of the ultimate legal effect given to a particular provision is, necessarily, whether the provision is unambiguous, defined by the court as "clearly worded and conspicuously displayed."[74] The Pennsylvania Supreme Court's opinion gave little guidance to aid in this determination. The court relied on the trial judge's conclusion that the language of the exclusions in the Standard Venetian Blind policy was "plain and free of ambiguity"[75] rather than announcing helpful guidelines upon which a future court could base its conclusion. In addition, the court's discussion of the conspicuously displayed requirement would be of minimal aid to a future court's decision making process since it offered only a cursory[76] explanation of the requirement that could be applied to nearly any modern standardized insurance contract.[77]

Although the court instructed that greater weight should be accorded the written language of an insurance policy, it also indicated that a judge may occasionally be justified in deviating from unambiguous language when interpreting an insurance contract.[78] In support of the latter proposition, the court cited the unconscionability provision of the Uniform Commercial Code,[79] which Pennsylvania has enacted.[80] Courts have generally chosen not to interpret the un-

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74. 503 Pa. at 307, 469 A.2d at 567.

75. *Id.* at 304, 469 A.2d at 565-66 ("The court of common pleas found that exclusions (n) and (o) set forth in the policy were 'plain and free of ambiguity,' and that these provisions expressly excluded coverage for damage to the portico."); *Id.* at 304, 469 A.2d at 566 ("As found by the court of common pleas, the exclusions at issue are 'plain and free of ambiguity,' and could have been readily comprehended by Mr. Morris had he chosen to read them.").

76. This statement provided the only indicia of reasoning behind the court's conclusion that the policy provisions were conspicuously displayed: "Immediately below the coverage provision was a section captioned 'Exclusions.' Under this section, conspicuously displayed and sequentially listed, were set forth the types of claims and losses for which American [Empire Insurance] was not obligated to defend or indemnify [Standard] Venetian [Blind]." *Id.* at 303, 469 A.2d at 565.

77. See the standard policies appended to Elliott, *supra* note 9, at 12-21 to 12-89.

78. 503 Pa. at 307, 469 A.2d at 567.

79. *See* U.C.C. § 2-302 (1978).

80. 13 PA. CONS. STAT. ANN. § 2302 (Purdon Supp. 1984). The provision provides:

> (a) Finding and authority of court. — If the court as a matter of law finds the contract or any clause of the contract to have been unconscionable at the time it was made, the court may:
>
> (1) refuse to enforce the contract;(2) enforce the remainder of the contract without the unconscionable clause; or(3) so limit the application of any unconscionable clause as to avoid any unconscionable result.
>
> (b) Evidence by parties — When it is claimed or appears to the court that the contract or any clause thereof may be unconscionable the parties shall be afforded a reasonable opportunity to present evidence as to its commercial setting, purpose and effect to aid the court in making the determination.

Although the provision applies only to sales of goods, 13 PA. CONS. STAT. ANN. § 2102 (Purdon 1984), the court must have meant that the contractual unconscionability concept would apply to insurance policies by analogy. *Cf.* Stanley A. Klopp, Inc. v. John Deere Co., 510 F. Supp. 807 (E.D. Pa. 1981) (law developed under U.C.C. unconscionability provision used to test authorized dealership agreement for unconscionability).

conscionability doctrine broadly, using unconscionability to find evidence of defect in contract formation rather than to strike down a contract provision when the substantive effect is unfair.[81] The Pennsylvania Supreme Court has followed this approach, requiring both an absence of meaningful choice in formation and oppressive substantive terms.[82] Therefore, the majority justices' citation to the unconscionability provision indicates the narrowness of the scope of judicial control that may be exerted by the Pennsylvania judiciary.[83]

The concurring and dissenting justices found the majority's traditional approach harsh and inappropriate for analysis of modern insurance contracts. The concurring justices favored the reasonable expectations doctrine,[84] and would have found for the insurer since they believed that a reasonable businessman would not have expected that his insurer would act as guarantor of the quality of his workmanship.[85] Justice Nix, dissenting, preferred application of the *Hionis* standard[86] and would have ruled for the insured since the insurer failed to prove that the policyholder was aware of the existence and effect of the exclusions.[87]

As a result of *Standard Venetian Blind*, lower courts will be less free to openly acknowledge the reasoning they use when fairness dictates a ruling in favor of the insured. Although the *Hionis* standard, which confronts insurance companies with serious practical problems, was destined to be overruled, the Pennsylvania Supreme Court overreacted to these shortcomings by instructing that traditional contract interpretive techniques should be employed in insurance policy coverage cases. Lower courts are likely to revert to their pre-*Hionis* technique of straining to find an ambiguity in straightforward language when fairness requires a ruling in favor of an insurance consumer.

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81. Comment, *supra* note 25, at 1157-59; *see also* Price, *The Conscience of Judge and Jury: Statutory Unconscionability as a Mixed Question of Law and Fact*, 54 TEMP. L.Q. 743, 757-58 (1981).

82. Witner v. Exxon, 495 Pa. 540, 434 A.2d 1222 (1981); *accord* Stanley A. Klopp, Inc. v. John Deere Co., 510 F. Supp. 807 (E.D. Pa. 1981); Evanoff v. York Fed. Sav. and Loan, 98 Dauphin Co. Rep. 49 (1975); *see also* Melso v. Texaco, 532 F. Supp. 1280 (E.D. Pa. 1982).

83. In Price, *supra* note 81, the author criticizes U.C.C. § 2-302 for achieving no predictability of results despite the aim of the drafters. If this criticism is accepted, use of the unconscionability doctrine would be inconsistent with one of the stated policy objectives put forth by the *Standard Venetian Blind* court. *See supra* notes 70-72 and accompanying text.

84. *See supra* notes 42-51 and accompanying text.

85. 503 Pa. at 307-08, 469 A.2d at 567 (Hutchinson, J., concurring).

86. *See supra* notes 55-64 and accompanying text.

87. 503 Pa. at 321, 469 A.2d at 574 (Nix, J., dissenting).

[Casenote by Karl A. Thallner, Jr.].

TORTS—MENTAL DISTRESS—MISSOURI REDEFINES THE STANDARD OF RECOVERY FOR NEGLIGENTLY INFLICTED EMOTIONAL DISTRESS ABSENT PHYSICAL IMPACT OR SUBSEQUENT PHYSICAL CONSEQUENCE. *Bass v. Nooney Co.*, 646 S.W.2d 765 (Mo. 1983) (en banc).

In *Bass v. Nooney Co.*,[1] a divided[2] Missouri Supreme Court abandoned the application of the "impact rule"[3] in emotional distress cases.[4] The court analyzed and rejected the frequently stated rationale supporting the impact rule,[5] and ultimately concluded that the automatic denial of mental distress claims absent proof of contemporaneous injury was inequitable, impractical, and illogical.[6] The court also declined to impose a standard of recovery which would require the plaintiff to prove that he suffered physical harm as a consequence of the mental or emotional distress.[7] In reaching its conclusion, the court recognized the need to limit its new rule[8] and,

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1. 646 S.W.2d 765 (Mo. 1983) (en banc).

2. Judge Wasserstrom wrote the majority opinion and was joined by Senior Judge Seiler and Judges Higgins and Gunn. Judges Welliver and Donnelly filed separate dissenting opinions.

3. Under the physical injury rule, otherwise known as the "impact rule", "[t]o sustain recovery for emotional distress and bodily harm resulting therefrom, plaintiff must suffer a traumatic physical injury through the fault of defendant, unless there is extreme and outrageous conduct on the part of the defendant intentionally or recklessly causing the emotional distress." Williams v. School Dist., 447 S.W.2d 256, 266 (Mo. 1969). *See* Victorian Ry. Comm'rs v. Coultas, 13 App. Cas. 222 (1888) (damages for mental shock arising from fear unaccompanied by physical injury were too remote); Mitchell v. Rochester Ry. Co., 151 N.Y. 107, 45 N.E. 354 (1896) (no recovery for injuries sustained by fright occasioned by the negligence of another where there is no immediate personal injury); Spade v. Lynn & B.R.R., 168 Mass. 285, 47 N.E. 88 (1897) (no recovery for fright, terror, alarm, anxiety, or distress of mind absent impact). *See generally Torts—Negligence—Direct Impact Rule*, 39 TEMP. L.Q. 229 (1966).

4. The court used the terms "mental" distress and "emotional" distress interchangeably. Medically speaking, mental distress resulting from a negligent act may be defined as a reaction to a traumatic stimulus. A traumatic stimulus can be defined as an impact, force, or event which affects an individual for either a brief or extended period of time, and can be physical or purely psychic. *See* Prosser, *Insult and Outrage*, 44 CALIF. L. REV. 40, 43 (1956); Smith & Solomon, *Traumatic Neurosis in Court*, 30 VA. L. REV. 87, 123 (1944). *See generally* M. MCLEAN, LEGAL ISSUES IN MEDICINE (1981); LAUGHLIN, *Neurosis Following Trauma*, in 6 TRAUMATIC MEDICINE AND SURGERY FOR THE ATTORNEY 76 (P. Cantor ed. 1962). For an explanation of the legal implications of the term "mental" or "emotional" distress, see *infra* note 9.

5. *See infra* notes 83-87, 91-96, 101-04 and accompanying text.

6. *Bass*, 646 S.W.2d at 772.

7. *Id. See infra* notes 46-58, 108-13 and accompanying text.

8. *Id.* at 772-73. The court appreciated the need to prevent undue extension of liability and, therefore, predicated recovery upon both the foreseeability and severity of the mental harm. *Id.*

therefore, refused to extend liability to include cases in which a plaintiff suffers inconsequential injury.[9] An individual who suffers from mental distress allegedly caused by the negligence of another will be permitted to recover for this distress, absent a showing of physical impact or subsequent physical injury, provided that the defendant should have known his actions would create an unreasonable risk of causing distress and the emotional distress is of sufficient severity to be both medically diagnosable and medically significant.[10]

Collette Bass was employed as a relief receptionist[11] by General Dynamics Company, which occupied several floors of a building owned and operated by the Nooney Company. On April 6, 1976, at approximately 11:15 a.m.,[12] Bass entered an elevator on the twentieth floor of the office building to ascend to the twenty-third floor. The elevator started moving upward but soon came to a grinding stop. Bass waited momentarily and then began pushing the emergency button, pounding on the elevator door, and shouting for help. The building maintenance workers eventually freed Bass one-half hour after the elevator stalled. Immediately following the incident, Bass was visibly shaken and distraught; and subsequently was advised to go to the area hospital.[13] Bass remained in the hospital for five days and did not return to work until May 2, 1976, nearly one month after the incident. The attending psychiatrist at the hospital[14]

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9. *Id.* The term "threshold tort" refers to the minimum requirements needed to establish a defendant's liability for emotional harm. The legal definition and interpretation of "emotional harm" dictates what these minimum requirements will be. The plaintiff must prove medical harm to the degree required by law, but this burden is difficult to meet in mental distress cases because the term "mental distress" has varying legal interpretations, which result in varying limits of emotional tort liability. Several authorities stress the need for a definition of "emotional harm" which excludes mere upset, dismay, humiliation, grief, and anger. At a minimum, emotional harm needed to support a threshold tort may include shock, continued nervousness, sleeplessness, or nausea that requires medication. Serious disorders and neuroses also satisfy the requirement. This is a clouded area of the law that only recently is becoming more clearly defined and standardized. *See generally* Comment, *Negligence and the Infliction of Emotional Harm: A Reappraisal of the Nervous Shock Cases*, 35 U. CHI. L. REV. 512 (1968); Comment, *Negligently Inflicted Mental Distress: The Case for an Independent Tort*, 59 GEO. L.J. 1237 (1971); Comment, *Molien v. Kaiser Foundation Hospitals: California Expands Liability for Negligently Inflicted Emotional Distress*, 33 HASTINGS L.J. 291 (1981); RESTATEMENT (SECOND) OF TORTS § 436A comment c (1979).

10. *Bass*, 646 S.W.2d at 772-73.

11. Bass' duties consisted, in part, of covering for various company secretaries during these secretaries' periodic rest breaks and lunch breaks. *Id.* at 766.

12. The Missouri Supreme Court noted that at another point in her testimony, Bass estimated that she had entered the elevator "at about quarter of eleven." *Id.* Bass was confined in the elevator for a period between one-half hour and one hour.

13. On April 7, 1976, the day following the incident, Bass entered another elevator in the building and collapsed. A Nooney company doctor escorted her to the hospital. The hospital record showed "she had experienced acute anxiety, slurred speech, her equilibrium was off, she felt light-headed, cold and thoroughly frightened, and too scared to sleep the night before." *Id.* at 767. Bass claimed that the confinement caused her to feel tense and strange in elevators and cars, and to lose her patience more often than she did before the incident. *Id.*

14. Dr. Hartnett testified that although Bass "had objective symptoms of anxiety, hyperhidroses of her palms, she was hyperventilating, her pupils were dilated, and her walking

testified with medical certainty[15] that Bass suffered from a severe anxiety reaction[16] precipitated by her confinement in the elevator.

Bass sought damages for fright and mental distress caused by the alleged negligence of both the Nooney Company and the Otis Elevator Company.[17] At the close of plaintiff's evidence, the trial court, applying the impact rule, sustained the defendants' motion to dismiss.[18] The Missouri Court of Appeals for the Eastern District also applied the impact rule and affirmed the lower court decision.[19] The plaintiff appealed to the Supreme Court of Missouri which identified the issues in the case to be first, whether plaintiff could rely on the principal of *res ipsa loquitur*[20] to establish defendants' negligence[21] and second, whether the application of the impact rule should be reconsidered and changed.[22]

Although the law readily protects an individual's physical and economic well-being from destructive interference, it is largely unwilling to allow recovery for detrimental interference with mental capacity.[23] Traditionally, an individual has been able to recover

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was unstable," she would not, in his opinion, suffer "permanent disability." *Id.* For a discussion of the medical meanings of these terms, see generally R. GRAY, ATTORNEY'S TEXTBOOK OF MEDICINE (3d ed. 1983).

15. An expert is often asked to testify in court to determine facts or resolve doubts regarding difficult issues within his sphere of special knowledge. Medical experts usually are called to reinforce or dispute the causal relationship between an accident and the alleged resultant injury. Based upon the expert's individual knowledge and review of all records and evidence, the expert then makes a determination, to the best of his medical ability, as to the cause of the alleged disability. For a thorough discussion of the medical expert in court, see generally E. GORDON, A PRACTICAL MEDICO-LEGAL GUIDE FOR THE PHYSICIAN (1973); 1 J. SCHMIDT, ATTORNEY'S DICTIONARY OF MEDICINE AND WORD FINDER (1982); 2 LAWYERS' MEDICAL CYCLOPEDIA OF PERSONAL INJURIES AND ALLIED SPECIALTIES §§ 13.1-13.98 (rev. vol. 1979).

16. Anxiety can be defined as a state of mind characterized by apprehension as well as unreasonable or vague fear. The condition usually is accompanied by restlessness, uncertainty, indecision, irritability, mental depression and, at times, shortness of breath, nausea, and rapid heart beat. During an anxiety reaction, the trauma produces acute tension that results in symptoms which are typically real, identifiable, and can be disabling. For an excellent review of both legal and medical implications of mental distress see J. SCHMIDT, *supra* note 15; Comment, *Negligently Inflicted Mental Distress: The Case for an Independent Tort*, *supra* note 9; LAUGHLIN, *Neurosis Following Trauma*, *supra* note 4.

17. The Otis Elevator Company, manufacturer of the malfunctioning elevator, was joined as a defendant along with the Nooney Company. *Bass*, 646 S.W.2d at 768.

18. The trial court entered a directed verdict for defendants on the ground that plaintiff suffered no impact. *Id.* at 766. The trial court opinion was not reported.

19. The court of appeals based its decision on the fact that the plaintiff was not thrown against the elevator and her "slight, trivial, minor physical contacts with the elevator when she pushed the emergency bell button . . . were insufficient to constitute the 'traumatic physical injury' required . . . to activate the physical rule." Bass v. Nooney Co., 646 S.W.2d 765, 780 (Mo. App. 1983) (en banc). Furthermore, the malfunction was so minor that the distress probably was caused by Bass' impending divorce, and her obligation to take care of her mother, a recent stroke victim. *Id.*

20. *See infra* notes 74-80 and accompanying text. The court considered this issue to be ancillary to the main issue concerning the impact rule.

21. *Bass*, 646 S.W.2d at 767.

22. *Id.* at 767-68.

23. It often has been stated that mental disturbances are not equivalent in severity to confirmed physical injuries, or injuries that are accompanied by physical manifestations and symptoms:

damages for mental distress only if he could demonstrate that the distress was intentionally inflicted,[24] the evidence supported an independent cause of action in tort or contract,[25] or the requirements of the impact rule were satisfied.[26] Under the impact rule, plaintiffs who have not suffered an actual physical impact to their person by the negligent force of another are denied the right to maintain a cause of action for the negligent infliction of emotional distress.[27] Both courts' and plaintiffs' dissatisfaction with the impact rule's stringent prerequisites for recovery prompted many jurisdictions to create and employ various liberalized standards of recovery in mental distress cases.[28] The impact rule — long the subject of frequent criticism[29] — has been abandoned in nearly all jurisdictions in

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> This distinction is based upon the ground that in an action for a bodily injury or illness resulting from a mental or emotional disturbance, the basis of the action is the bodily injury or illness, an interest always afforded protection by law, while the mental or emotional disturbance, an interest not generally afforded independent protection by law, is merely a link in the chain of causation.

38 AM. JUR. 2D *Fright, Shock, Etc.* § 18 (1968). *See also* Spade v. Lynn & B.R.R., 168 Mass. 285, 47 N.E. 88 (1897).

24. Until the 1930's, recovery for emotional distress was generally allowed only in connection with traditional intentional torts such as assault, battery, false imprisonment, trespass, malicious prosecution, nuisance, seduction, conversion, invasion of privacy, and defamation. *See* PROSSER, HANDBOOK OF THE LAW OF TORTS 28-49 (4th ed. 1971). At one time, intentional infliction of emotional distress was not recognized as an independent tort, therefore, emotional distress damages were considered to be parasitic damages. All states now recognize the intentional infliction of emotional distress as an independent tort, and allow recovery for severe emotional distress, disturbance, fright or shock intentionally caused by extreme and outrageous conduct. Recovery is allowed despite absence of physical injury or impact. *See* State Rubbish Collectors Ass'n v. Siliznoff, 38 Cal.2d 330, 240 P.2d 282 (1952);Smith v. Aldridge, 356 S.W.2d 532 (Mo. App. 1962); M.B.M. Co. v. Counce, 268 Ark. 629, 596 S.W.2d 681 (1980); Sheltra v. Smith, 136 Vt. 472, 392 A.2d 431 (1978); Zimmerman v. Associates Discount Corp., 444 S.W.2d 396 (Mo. 1969); *cf.* Bencomo v. Morgan, 210 So. 2d 236 (Fla. Dist. Ct. App. 1968) (no recovery against defendant-doctor who agreed to support a petition to have plaintiff declared incompetent); Deming v. Kellogg, 41 Colo. App. 264, 583 P.2d 944 (1978) (mere occurrence of an accident did not necessarily mean that outrageous conduct was present); Rawson v. Sears Roebuck & Co., 530 F. Supp. 776 (D. Colo. 1982) (no recovery against defendant-employer who allegedly willfully, wantonly, and maliciously fired the plaintiff). *See generally* RESTATEMENT (SECOND) OF TORTS §§ 46, 546 (1965).

25. *See* Schmitz v. St. Louis, I.M. & S.R.R., 119 Mo. 256, 24 S.W. 472 (1893); Frewen v. Page, 238 Mass. 499, 131 N.E. 475 (1921); Guillory v. Godfrey, 134 Cal. App. 2d 628, 286 P.2d 474 (1955); Lamm v. Shingleton, 231 N.C. 10, 55 S.E.2d 810 (1949); Stewart v. Rudner, 349 Mich. 459, 84 N.W.2d 816 (1957). *See generally* MCCORMICK, HANDBOOK ON THE LAW OF DAMAGES § 145 (1935).

26. *See supra* note 3. *See infra* notes 35-42 and accompanying text.

27. *See infra* notes 35-42 and accompanying text.

28. *See, e.g.*, Robb v. Pennsylvania R.R., 58 Del. 454, 210 A.2d 709 (1965); Battalla v. State, 10 N.Y.2d 237, 176 N.E.2d 729, 219 N.Y.S.2d 34 (1961); Dziokonski v. Babineau, 375 Mass. 555, 380 N.E.2d 1295 (1978); Falzone v. Busch, 45 N.J. 559, 214 A.2d 12 (1965). *See infra* notes 46, 49, 52, 58-60 and 67 and accompanying text.

29. The impact rule has come under extensive scholarly criticism expressed through a multitude of articles written on the subject. *See* Prosser, *Insult and Outrage*, 44 CALIF. L. REV. 40 (1956); Prosser, *Intentional Infliction of Mental Suffering: A New Tort*, 37 MICH. L. REV. 874 (1939); Comment, *negligently Inflicted Mental Distress: The Case For An Independent Tort*, *supra* note 9; Note, *Mental Distress—The Impact Rule*, 42 UMKC L. REV. 234 (1973); Note, *Redefining the Limits to Recovery for Negligently Inflicted Mental Distress*, 11 TULSA L.J. 587 (1976); Comment, *Mental Distress as an Actionable Tortious Wrong*, 37 UMKC L. REV. 371 (1969).

the United States.[30]

American courts have expressed differing views concerning recovery for mental distress absent physical impact.[31] These varying positions have resulted, in large part, from the diverse methods courts have developed to analyze the concepts of duty, foreseeability, and proximate cause.[32] Traditionally, conservative courts considered the duty owed by negligent defendants to victims of mental distress to be greatly limited or nonexistent.[33] These jurisdictions have followed the impact rule long after most liberal jurisdictions expanded the scope of recovery in mental distress cases.[34]

The leading case applying the impact rule to negligent infliction of emotional distress cases is the 1888 decision of *Mitchell v. Rochester Railway*.[35] The reasoning in *Mitchell* set forth the idea that "[a]ssuming that fright cannot form the basis of an action, it is obvious that no recovery can be had for injuries resulting therefrom."[36] The *Mitchell* court concluded that because a cause of action could not be maintained for fright alone, the severity of the resultant injury was irrelevant.[37] The court, relying on public policy considerations,[38] also reasoned that the plaintiff's injuries were not within the

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30. W. PROSSER, HANDBOOK OF THE LAW OF TORTS § 54 (4th ed. 1971) [hereinafter cited as PROSSER]. Prosser lists the states of Arkansas, Illinois, Indiana, Kentucky, Maine, Massachusetts, Michigan, Missouri, Ohio, Virginia, and Washington as states that adhere to the impact rule. *Id.* Since that listing, the number of adherents has decreased. Recent decisions indicate that the following states have rejected the impact rule: Maine in Wallace v. Coca-Cola Bottling Plants, Inc., 269 A.2d 117 (Me. 1970); Massachusetts in Dziokonski v. Babineau, 375 Mass. 555, 380 N.E.2d 1295 (1978); Michigan in Daley v. LaCroix, 384 Mich. 4, 179 N.W.2d 390 (1970); Ohio in Schultz v. Barberton, 4 Ohio St. 3d 131, 447 N.E.2d 109 (1983); Virginia in Hughes v. Moore, 214 Va. 27, 197 S.E.2d 214 (1973); and Washington in Schurk v. Christensen, 80 Wash. 2d 652, 497 P.2d 937 (1972).

31. *See supra* notes 28-30 and accompanying text.

32. *See generally* PROSSER, *supra* note 30, at 327-35; Comment, *Negligently Inflicted Mental Distress: The Case for an Independent Tort*, *supra* note 9.

33. *See supra* note 32.

34. *See supra* note 30. (Note, unless otherwise stated, the phrase "victims of mental distress" denotes victims who suffered no contemporaneous physical impact or injury. The phrase shall have this meaning with regard to "impact rule" analysis only).

35. 151 N.Y. 107, 45 N.E. 354 (1896).

36. *Id.* at 354. In the *Mitchell* case, the court denied recovery for mental distress, which was allegedly caused by the defendant's negligent operation of a team of horses, that ultimately resulted in plaintiff's miscarriage. The *Mitchell* decision was inspired by the 1888 British case of Victorian Ry. Comm'rs v. Coultas, 13 App. Cas. 222 (1888). In that case, the Privy Council concluded that damages for shock arising from fear unaccompanied by physical injury were too remote and could not "be considered a consequence which, in the ordinary course of things, would flow from the negligence . . . ." *Id.* at 225. The *Coultas* decision was expressly overruled thirteen years later in the case of Dulieu v. White & Sons, 2 K.B. 669 (1901) (court permitted a cause of action for serious illness and the premature birth of plaintiff's baby resulting from distress, which was caused by defendant's negligent operation of his horse-drawn van).

37. *Mitchell*, 151 N.Y. at 107, 45 N.E. at 354. "That the result may be nervous disease, blindness, insanity, or even a miscarriage, in no way changes the principle. These results merely show the degree of fright, or the extent of damages." *Id.*

38. *See infra* notes 41-42 and accompanying text.

rule of proximate damages and, therefore, were not recoverable.[39]

By 1930, a majority of American courts had adopted the *Mitchell* rationale and thirty-one jurisdictions had implemented laws resembling the impact rule.[40] Justifications in support of the impact rule originally set forth in *Mitchell* were later reiterated clearly and concisely by the Pennsylvania Supreme Court in *Niederman v. Brodsky*.[41] The court enunciated the following justifications for the rule's existence: the difficulty medical science would have proving a causal relation between the subjective symptoms of distress and the defendant's alleged negligent act; the possibility of an increased number of fictitious injuries and fraudulent claims; and the possibility that extending the boundaries of recovery would cause a flood of litigation.[42] After 1930, however, several jurisdictions refused to adopt the impact rule and many courts that previously accepted the rule began to question its utility.[43] In response to increased criticism, courts began to allow recovery for mental distress in cases in which plaintiffs proved extremely slight impact.[44] These sympathetic efforts by the

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39. *Mitchell*, 151 N.Y. at 107, 45 N.E. at 355. The rule of proximate damages states that these damages are the ordinary and natural results of the negligence charged and, therefore, are reasonably expected. *Id.* Injuries that are the result of accidental or unusual circumstances cannot be anticipated or controlled by the defendant and are too remote to form a cause of action for relief. *Id.*

40. *See* Note, *Mental Distress—The Impact Rule*, 42 UMKC L. REV. 234 (1973).

41. 436 Pa. 401, 261 A.2d 84 (1970) (plaintiff-pedestrian suffered a severe heart attack after defendant-motorist skidded onto the sidewalk, struck his son, and nearly hit the plaintiff). The *Niederman* court analyzed and rejected the three traditional policy arguments stated in support of the impact rule. The court chose to abandon the requirement of physical impact as a prerequisite for recovery of damages proximately caused by the negligence of the named defendant. *Id.* at 406, 261 A.2d at 90. The court limited the rule to cases in which the plaintiff was in personal danger of physical impact "because of the direction of a negligent force against him and where plaintiff actually did fear the physical impact." *Id.*

42. *Id.* at 405-13, 261 A.2d at 86-90. For an in-depth analysis and criticism of each of the three policy justifications see, *e.g.*, Sinn v. Burd,, 486 Pa. 146, 404 A.2d 672 (1979); Tobin v. Grossman, 24 N.Y.2d 609, 249 N.E.2d 419, 301 N.Y.S.2d 554 (1969); Falzone v. Busch, 45 N.J. 559, 214 A.2d 12 (1965); Okrina v. Midwestern Corp., 282 Minn. 400, 165 N.W.2d 259 (1969); Robb v. Pennsylvania R.R., 58 Del. 454, 210 A.2d 709 (1965); Leong v. Takasaki, 55 Hawaii 398, 520 P.2d 758 (1974); Culbert v. Samson's Supermarkets Inc., 444 A.2d 433 (Me. 1982); Hughes v. Moore, 214 Va. 27, 197 S.E.2d 214 (1973); Stewart v. Gilliam, 271 So.2d 466 (Fla. Dist. Ct. App. 1972); Schultz v. Barberton, 4 Ohio St. 3d 131, 447 N.E.2d 109 (1983), Battalla v. State, 10 N.Y.2d, 237, 176 N.E.2d 729, 219 N.Y.S.2d 34 (1961).

43. *See supra* notes 28-30 and accompanying text.

44. *See, e.g.*, Porter v. Delaware L.&W.R.R., 73 N.J.L. 405, 63 A. 860 (1906) (dust in the eye sufficient impact); Kenney v. Wong Len, 81 N.H. 427, 128 A. 343 (1925) (mousehair in stew touching roof of plaintiff's mouth); Jansen v. Minneapolis St. L. Ry., 112 Minn. 496, 128 N.W. 826 (1910) (hitting plaintiff over the head with a hat); McCardle v. George B. Peck Dry Goods Co., 191 Mo. App. 263, 177 S.W. 1095 (1915) (slight jar sufficient impact); Morton v. Stack, 122 Ohio St. 115, 170 N.E. 869 (1930) (child inhaled smoke while trapped in a burning building); Zelinsky v. Chimics, 196 Pa. Super. 312, 175 A.2d 351 (1961) (impact of car's collision sufficient). *But see* Koplin v. Louis K. Liggett Co., 332 Pa. 333, 185 A. 744 (1936) (nausea over presence of centipede in soup not sufficient); Tuttle v. Meyer Dairy Products Co., 138 N.E.2d 429 (Ohio Ct. App. 1956) (no impact when glass was found in mouth while eating); Hamilton v. Pepsi-Cola Bottling Co., 132 A.2d 500 (D.C. 1957) (no recovery for drinking softdrink containing matches).

courts to avoid the doctrine, however, did not alleviate the rule's harsh effect of denying claims to those individuals who suffered merely mental distress.[45] In light of courts' efforts to evade the doctrine, abandonment of the impact rule was inevitable.

In an effort to remedy the inequities associated with the impact rule, a majority of courts began to allow recovery for physical harm suffered as a consequence of mental or emotional distress.[46] This standard, which incorporates the underlying rationale of the impact rule, also is designed to protect against frivolous or fraudulent claims by requiring proof of the physical manifestation of the psychic injury before recovery will be granted.[47] The rule is applied in cases that usually arise in one of two contexts. In the first situation, the defendant is liable if his negligent act causes mental or emotional distress that he realized or should have realized would result in plaintiff's illness or bodily harm.[48] In order for the plaintiff to recover, the negligent infliction of emotional distress must result in demonstrable bodily harm. Without proof of resultant injury, mental distress fails to afford a basis for a cause of action.[49]

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45. That physical impact is required, no matter how trivial, effectively denies recovery to plaintiffs or witnesses who have suffered impacts solely in the sense of emotional upset or disturbance. *See generally* Note, *Redefining the Limits to Recovery for Negligently Inflicted Mental Distress*, *supra* note 29.

46. *See, e.g.*, Bowman v. Williams, 164 Md. 397, 165 A. 182 (1933) (recovery granted where clear and substantial physical injury results from frights); Bedenk v. St. Louis Pub. Serv. Co., 285 S.W.2d 609 (Mo. 1955) (physical injury includes physical shock or physical wounds or bruises); Falzone v. Busch, 45 N.J. 559, 214 A.2d 12 (1965) (recovery granted for bodily injury or sickness resulting from plaintiff's fear of defendant's negligently driven auto); Crews v. Provident Fin. Co., 271 N.C. 684, 157 S.E.2d 381 (1967) (defendant caused plaintiff's heart attack and elevated blood pressure when he used vulgar language to threaten plaintiff); Vance v. Vance, 286 Md. 490, 408 A.2d 728 (1979) (plaintiff's emotional collapse and depression which were manifested in symptoms of spontaneous crying, shock, and ulcer constituted sufficient physical injury). *But see, e.g.*, Wedgworth v. Ft. Worth, 189 S.W.2d 40 (Tex. Civ. App. 1945) (loss of memory and ability to concentrate were not physical injuries); Cosgrove v. Beymer, 244 F. Supp. 824 (D. Del. 1965) (dizziness, headaches, and nervousness accompanying shock did not compose bodily harm); Lessard v. Tarca, 20 Conn. Supp. 295, 133 A.2d 625 (1957) (mental anguish and pain resulting from parents and child watching another child burn to death not recoverable). For an in-depth analysis of the difficulty surrounding differences between mental and physical injury, see generally Comment, *Negligently Inflicted Mental Distress: The Case for an Independent Tort*, *supra* note 9.

47. *See supra* note 46.

48. RESTATEMENT (SECOND) OF TORTS §§ 306, 312, 313, 436(1) (1965).

49. In this context, the individual is not threatened by possible contemporaneous physical impact. The mental distress only becomes important if it results in physical injury. *E.g.*, Kuhr Bros. Inc. v. Spahos, 89 Ga. App. 885, 81 S.E.2d 491 (1954) (no recovery for father's fright experienced while attempting to rescue son from burning house); Kaufman v. Israel Zion Hosp., 183 Misc. 714, 51 N.Y.S.2d 412 (1944) (no recovery for mental suffering caused by a hospital telling parents their newborn was a girl and later telling them it was a boy); Espinosa v. Beverly Hosp., 114 Cal. App. 2d 232, 249 P.2d 843 (1952) (no recovery for delivery of wrong baby in hospital); Cushing Coca-Cola Bottling Co. v. Francis, 206 Okla. 553, 245 P.2d 84 (1952) (no recovery for mental distress caused by plaintiff's finding the partially decomposed body of a mouse in a coke bottle); Gambill v. White, 303 S.W.2d 41 (Mo. 1957) (no recovery for mental distress allegedly caused by defendant-hospital's failure to attend to plaintiff while she was giving birth). *But see, e.g.*, Montinieri v. Southern New England Tel. Co., 175 Conn. 337, 398 A.2d 1180 (1978) (recovery for emotional distress caused by defendant-

In the second situation, the plaintiff does fear for his own safety.[50] The theory applied under these circumstances has been labeled the "zone of danger rule."[51] Under this rule, liability is expanded to include cases in which the plaintiff observed either danger or actual injury to another, and simultaneously, both feared for his own safety and was within the same zone of physical danger as the victim.[52] Efforts to extend liability beyond the boundaries of the zone of danger[53] have repeatedly failed because courts fear there can be no reasonable, equitable manner in which to limit recovery.[54] The New York Court of Appeals in *Tobin v. Grossman*[55] recognized this need to limit the rule and stated, "[e]very injury has ramifying consequences, like the ripplings of the waters, without end. The problem for the law is to limit the legal consequences of wrongs to controllable degree. . . . It is enough that the law establishes liability in favor of those directly or intentionally harmed."[56] The problem of unlimited liability frequently is associated with standards of recovery in negligent infliction of mental distress cases. Often, because there is no ready solution to the problem, courts create arbitrary distinctions that merely replace erratically applied rules.[57] The possibility that

company's disclosure of plaintiff's address).

50. An event puts the plaintiff in a situation that poses the threat of immediate bodily impact or injury. *See infra* notes 52-56 and accompanying text.

51. *Id.*

52. *E.g.*, Amaya v. Home Ice, Fuel & Supply Co., 59 Cal. 2d 295, 379 P.2d 513, 29 Cal. Rptr. 33 (1963) (overruled by Dillon v. Legg, 68 Cal. 2d 728, 441 P.2d 912, 69 Cal. Rptr. 72 (1968)); Orlo v. Connecticut Co., 128 Conn. 231, 21 A.2d 402 (1941) (defendant's live trolley wires fell onto car in which plaintiff was riding); Netusil v. Novak, 120 Neb. 751, 235 N.W. 335 (1930) (shock caused by attack of vicious dog was actionable without presence of bite); Battalla v. State, 10 N.Y.2d 237, 176 N.E.2d 729, 219 N.Y.S.2d 34 (1961) (recovery for distress caused by defendant's failure to secure safety bar of ski-lift chair); Niederman v. Brodsky, 436 Pa. 401, 261 A.2d 84 (1970) (heart attack caused by stress occurring after defendant's auto nearly hit plaintiff was actionable); Falzone v. Busch, 45 N.J. 559, 214 A.2d 12 (1965) (recovery for shock resulting from defendant's negligent operation of auto close to plaintiff); Tobin v. Grossman, 24 N.Y.2d 609, 249 N.E.2d 419, 301 N.Y.S.2d 554 (1969) (recovery denied to plaintiff-mother who did not see defendant's auto hit child but arrived at the scene immediately thereafter); *cf.* Dziokonski v. Babineau, 375 Mass. 555, 380 N.E.2d 1295 (1978) (recovery granted to plaintiff-mother who did not see defendant's bus strike her child but arrived immediately thereafter).

53. *See supra* note 52. The "zone of danger" literally refers to the plaintiff's physical proximity to the victim of the actual impact.

54. *Id.* For the first time in negligence actions, this rule provided the plaintiff-bystander, who suffers mental distress caused by threatened impact, with an opportunity to recover for this emotional distress. *See* Amaya v. Home Ice, Fuel & Supply Co., 59 Cal. 2d 295, 379 P.2d 513, 2 Cal. Rptr. 33 (1963). *See also* Guilmette v. Alexander, 128 Vt. 116, 259 A.2d 12 (1969).

55. 24 N.Y.2d 609, 249 N.E.2d 419, 301 N.Y.S.2d 554 (1969).

56. *Id.* at 615, 249 N.E.2d at 424, 301 N.Y.S.2d at 561-62. The *Tobin* decision rejected Dillon v. Legg, 68 Cal. 2d 728, 441 P.2d 912, 69 Cal. Rptr. 72 (1968) (*see infra* notes 59-62 and accompanying text), and denied recovery to a bystander who was outside the zone of danger. The *Tobin* court conceded that the zone of danger requirement was an arbitrary limitation, but justified it as the only way to prevent unlimited liability. *Tobin*, 24 N.Y.2d at 616, 249 N.E.2d at 423, 301 N.Y.S.2d at 559.

57. *See generally* PROSSER, *supra* note 24, § 54. The RESTATEMENT (SECOND) OF TORTS originally included a caveat suggesting that a parent or spouse may be entitled to recov-

defendants would be exposed to unlimited liability, as well as the allegedly inconsistent nature[58] of the rule, have led some courts to reject the zone of danger rule in favor of more liberalized, flexible standards of recovery.

In 1968, the California Supreme Court specifically rejected the zone of danger rule in the case of *Dillon v. Legg*,[59] and became the first jurisdiction to hold that a plaintiff mother who witnessed the negligent infliction of death or injury to her child could recover for mental and subsequent physical distress.[60] The court granted recovery despite the fact that the plaintiff suffered no impact and was outside the zone of danger.[61] The *Dillon* decision emphasized the importance of the "foreseeability of the risk" and deemed it to be "the chief element in determining whether [the] defendant owes a duty or an obligation to [the] plaintiff."[62] The court then set forth three criteria to be used in analyzing the foreseeability issue: whether plaintiff was located near the scene of the accident; whether the shock resulted from a direct emotional impact upon the plaintiff from the sensory and contemporaneous observance of the accident; and whether the plaintiff and the victim were closely related.[63] The *Dil-*

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ery for mental harm suffered as a result of seeing injury to the child or other spouse. RESTATEMENT (SECOND) OF TORTS § 313 CAVEAT (1934). In the RESTATEMENT (SECOND) OF TORTS, the caveat was stricken, not because of direct opposition to the caveat, but because case law had established no liability under those circumstances. RESTATEMENT (SECOND) OF TORTS § 313 (1965); RESTATEMENT (SECOND) OF TORTS § 313 app. (1965).

58. *See infra* note 60 and accompanying text. Many courts considered the zone of danger rule to be as arbitrary and harsh as the impact rule. *See, e.g.*, Corso v. Merrill, 119 N.H. 647, 658, 406 A.2d 300, 307 (1979) ("zone of danger rule imposes unjust limitations on recovery"); Dziokonski v. Babineau, 375 Mass. 555, 564, 380 N.E.2d 1295, 1300 (1978) ("zone of danger rule . . . lacks strong logical support"); D'Ambra v. United States, 114 R.I. 643, 657, 338 A.2d 524, 531 (1975) ("zone of danger rule ignores psychological reality").

59. 68 Cal. 2d 728, 441 P.2d 912, 69 Cal. Rptr. 72 (1968).

60. *Id.* at 732-33, 441 P.2d at 915, 69 Cal. Rptr. at 75-76. The *Dillon* decision overruled Amaya v. Home Ice, Fuel & Supply Co., 59 Cal. 2d 295, 379 P.2d 513, 29 Cal. Rptr. 33 (1963); in which the California Supreme Court adhered to the impact rule. The *Dillon* court examined the facts of the case at bar and concluded that the application of the zone of danger rule would produce arbitrary and unjust results. The court stated:

> [w]e can hardly justify relief to the sister for trauma which she suffered upon apprehension of the child's death and yet deny it to the mother merely because of a happenstance that the sister was some few yards closer to the accident . . . . The instant case exposes the hopeless artificiality of the zone-of-danger rule.

Dillon at 733, 441 P.2d at 915, 69 Cal. Rptr. at 75.

61. *Dillon* at 732-33, 441 P.2d at 915, 69 Cal. Rptr. at 75-76.

62. *Id.* at 740, 441 P.2d at 920, 69 Cal. Rptr. at 80. The court, applying general tort law principles of negligence, proximate cause, and foreseeability, focused on whether the accident and resulting harm to the bystander were reasonably foreseeable. The *Dillon* decision contemplated "that courts in a case-to-case basis, analyzing all the circumstances, will decide what the ordinary man under such circumstances should have reasonably foreseen. The courts thus mark out the areas of liability, excluding the remote and unexpected." *Id.* at 741, 441 P.2d at 921, 69 Cal. Rptr. at 81. For the purposes of this casenote, the term "bystander" refers to anyone who sustains mental distress and possibly, resultant physical injury as a result of witnessing an injury to another, and is not limited to relatives of the victim who actually sustained the impact.

63. *Id.* at 740-41, 441 P.2d at 920, 69 Cal. Rptr. at 80. The evaluation of these factors

lon court expressly limited its rule to cases in which the plaintiff suffers physical injury as a consequence of emotional distress.[64]

Four years after the *Dillon* decision, the California Supreme Court decided the case of *Molien v. Kaiser Foundation Hospitals*.[65] The court distinguished the facts of the case from *Dillon*[66] and allowed recovery for severe emotional distress, despite the absence of impact or consequential physical injury, because the facts of the case guaranteed the claim's authenticity, and plaintiff's injuries were reasonably foreseeable to the defendant.[67] In formulating this standard, the *Molien* court relied heavily on *Rodrigues v. State*.[68] In *Rodrigues*, the Hawaii Supreme Court adopted the rule that recovery will be granted if the circumstances of the case provide some assurance that the plaintiff suffered serious mental injury resulting from defendant's negligence.[69] The *Molien* opinion indicated that the absence of immediate or consequential physical injury should not preclude possible claims for mental or emotional distress, particularly in negligence cases.[70] The holding in *Molien* has been criticized as ambigu-

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determines the degree of foreseeability which, in turn, depend upon the facts of each case. *Id.* Only Connecticut in D'Amicol v. Alvarez Shipping Co., 31 Conn. Supp. 164, 326 A.2d 129 (1973) has adopted the *Dillon* approach without modification. The majority of courts that have considered the *Dillon* rationale have rejected it. *See, e.g.*, Whetham v. Bismarck Hosp., 197 N.W.2d 678 (N.D. 1972); Jelley v. LaFlame, 108 N.H. 471, 238 A.2d 728 (1968); Grimsby v. Samson, 85 Wash. 2d 52, 530 P.2d 291 (1975); Tobin v. Grossman, 24 N.Y.2d 609, 249 N.E.2d 419, 301 N.Y.S.2d 554 (1969). Other jurisdictions have adopted the underlying policy of *Dillon*, but have imposed additional requirements. *See, e.g.*, Portee v. Jaffe, 84 N.J. 88, 417 A.2d 521 (1980); Leong v. Takasaki, 55 Hawaii 398, 520 P.2d 758 (1974); Sinn v. Burd, 486 Pa. 146, 404 A.2d 672 (1979).

64. *Dillon* at 740, 441 P.2d at 920, 69 Cal. Rptr. at 80.

65. 27 Cal. 3d 916, 616 P.2d 813, 167 Cal. Rptr. 831 (1980).

66. *Id.* at 921-23, 616 P.2d at 816, 167 Cal. Rptr. at 833-34. The *Molien* court recognized that in *Dillon*, the plaintiff sought recovery for damages she suffered as a result of witnessing injury to a third person; and the three guidelines listed were limitations on that particular cause of action. *Id.* In contrast, Mr. Molien was a "direct victim of the assertedly negligent act." *Id.* The *Molien* court applied only the *Dillon* rule's general principle of foreseeability to the facts of the case. *See infra* note 67 and accompanying text.

67. Molien v. Kaiser Found. Hosp., 27 Cal. 3d 916, 616 P.2d 813, 167 Cal. Rptr. 831 (1980). The plaintiff's wife underwent a physical examination in defendant-hospital during which lab tests were misread and plaintiff was told she had syphillis. The wife suspected that plaintiff had engaged in extramarital relations and the marriage broke up. Plaintiff sued for negligent infliction of emotional distress and loss of consortium. The court applied a traditional foreseeability test to the facts of the case and concluded that "[i]t is easily predictable that an erroneous diagnosis of syphillis and its probable source would produce marital discord and resultant emotional distress to a married patient's spouse." *Id.* at 923, 616 P.2d at 817, 167 Cal. Rptr. at 835. The risk of harm was reasonably foreseeable so defendant owed a duty to plaintiff to exercise care in making the diagnosis. *Id.*

68. 52 Hawaii 156, 472 P.2d 509 (1970). In *Rodrigues*, the plaintiffs sued for mental suffering resulting from residential flood damage allegedly caused by the defendant-state's negligence. The court allowed recovery, but limited the rule to cases in which the plaintiff suffers "serious emotional distress." Serious emotional distress occurs "[w]here a reasonable man, normally constituted, would be unable to adequately cope with the mental distress engendered by the circumstances of the case." *Id.* at 163, 472 P.2d at 520.

69. Rodrigues v. State, 52 Hawaii 156, 472 P.2d 509 (1970).

70. Molien v. Kaiser Found. Hosp., 27 Cal. 3d 916, 616 P.2d 813, 167 Cal. Rptr. 831 (1980). The court viewed the physical injury requirement as "both overinclusive and underinclusive when viewed in light of its purported purpose of screening false claims." *Id.* at 928, 616

ous, in that the court used expansive language to abandon the requirement of consequential physical injury, but appeared to leave the *Dillon* rule intact.[71] Despite the ambiguity, the *Molien* decision, at the very least, affords plaintiffs who suffer serious emotional distress[72] absent impact or consequential injury the opportunity to state their claims in court.[73] This was the state of emotional distress law that confronted the *Bass* court.

The *Bass* majority began its analysis with a brief discussion of the doctrine of *res ipsa loquitur*,[74] and that doctrine's applicability to the facts of the case. The court focused on three elements required to sustain a cause of action under *res ipsa loquitur*,[75] and determined that the plaintiff's evidence satisfied each of the elements.[76] The court also noted that the doctrine frequently has been applied in cases involving injuries caused by malfunctioning elevators.[77] The court first rejected the defendants' contention that the doctrine was inapplicable because the elevator did not lurch or move violently, stating that the stalling of the elevator was a "sudden unusual mal-

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P.2d at 820, 167 Cal. Rptr. at 838. The requirement is overinclusive in that any physical injury, no matter how trivial, suffices for recovery. It is underinclusive in that valid, possibly provable claims are denied at the pleading stage. *Id. Molien* applies to cases in which the plaintiff is a direct victim of negligence.

71. The three *Dillon* guidelines, *see supra* note 63 and accompanying text, appear to be intact. *See* Hathaway v. Superior Court, 112 Cal. App. 3d 728, 737, 169 Cal. Rptr. 435, 440 (1980). *See also* Cortez v. Macias, 110 Cal. App. 3d 640, 167 Cal. Rptr. 905 (1980). It appears that after *Molien*, the *Dillon* criteria are applicable only to "percipient witnesses" to injury (the bystander scenario).

72. *See supra* note 68.

73. *See generally* Comment, *Molien v. Kaiser Foundation Hospitals: California Expands Liability for Negligently Inflicted Emotional Distress*, *supra* note 9; Note, *Negligent Infliction of Emotional Distress Absent Physical Impact or Subsequent Physical Injury*, 47 MO. L. REV. 124 (1982).

74. The phrase "res ipsa loquitur" literally means "the thing itself speaks." The doctrine depends upon the strength of the inference that, given a certain injury, the defendant must have been negligent. The mere occurrence of certain events is held to present a prima facie case of negligence, which, unless defendant produces counter evidence that tends to show the absence of negligence, enables the court to find the defendant guilty of negligence without further proof. *See* BALLENTINE'S LAW DICTIONARY 1129 (3d ed. 1969). *See also* O'Dell v. Whitworth, 618 S.W.2d 681 (Mo. App. 1981) (evidence must reasonably exclude the negligence of the injured party as a contributing cause); Harke v. Haase, 335 Mo. 1104, 75 S.W.2d 1001 (1934) (prima facie case raises a substantial factual inference of defendant's negligence which amounts to evidence, not presumption); *see generally* PROSSER, *supra* note 24, § 39.

75. *Res ipsa loquitur* applies when: (a) the occurrence resulting in injury does not ordinarily occur if those in charge use due care; (b) the instrumentalities involved were under the management and control of the defendant; and (c) the defendant possesses superior knowledge or means of information as to the cause of the occurrence. PROSSER, *supra* note 24, § 39. For a discussion of each element see McCloskey v. Koplar, 329 Mo. 527, 46 S.W.2d 557 (1932); Davis v. Jackson, 604 S.W.2d 610 (Mo. App. 1980); Neis v. National Super Mkt. Inc., 631 S.W.2d 690 (Mo. App. 1982); Strick v. Stutsman, 633 S.W.2d 148 (Mo. App. 1982). *See generally* 5 WIGMORE ON EVIDENCE § 2509 (2d ed. 1935).

76. Bass v. Nooney Co., 646 S.W.2d at 768.

77. *Id. See, e.g.*, Stroud v. Booth Cold Storage Co., 285 S.W. 165 (Mo. App. 1926); Blanton v. Dold, 109 Mo. 64, 18 S.W. 1149 (1892); Meade v. Missouri Water & Steam Supply Co., 318 Mo. 350, 300 S.W. 515 (1927); Warner v. Terminal R.R. Ass'n, 363 Mo. 1082, 257 S.W.2d 75 (1953); Bartlett v. Pontiac Realty Co., 224 Mo. App. 1234, 31 S.W.2d 279 (1930).

function which would not normally occur without negligence of the parties in charge."[78] The fact that two parties were joined as defendants did not bar the application of *res ipsa loquitur* in the *Bass* case because the jury could reasonably conclude that either or both of the defendants were in control of the elevator.[79] The majority briefly dismissed this ancillary issue,[80] and then addressed the applicability of the impact rule.

The *Bass* decision ended the century-long adherence to the impact rule in mental distress cases in the state of Missouri.[81] The *Bass* majority, after painstakingly reviewing the general history of the impact rule,[82] reasoned that the rule was entirely too rigid in its application. The majority predicated this determination upon a careful analysis, and subsequent rejection of the three reasons traditionally stated in support of the impact rule.[83]

The supposition that medical science is unable to prove a causal connection between the alleged damage to the plaintiff and the negligent act that supposedly induced the mental or emotional distress, has long afforded justification for the impact rule.[84] The *Bass* majority refused to accept this rationale and relied on two factors to support its conclusion. First, the court pointed to the enormous advances in the medical field that have "enabled science to establish with reasonable medical certainty the existence and severity of psychic harm."[85] Second, the majority, relying on the decision in *Niederman v. Brodsky*,[86] concluded that although it still may be difficult for

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78. Bass v. Nooney Co., 646 S.W.2d at 768.

79. *Id. See* Greet v. Otis Elevator Co., 187 A.2d 896 (Colo. Ct. App. 1963); Willis v. Terminal R.R. Ass'n, 421 S.W.2d 220 (Mo. 1967); Corcoran v. Banner Super Mkt., Inc., 19 N.Y.2d 425, 227 N.E.2d 304, 280 N.Y.S.2d 385 (1967); Crystal Tire Co., v. Home Serv. Oil Co., 465 S.W.2d 531 (Mo. 1971). *See generally* 5 PERSONAL INJURY: ACTIONS, DEFENSES, DAMAGES § 1.07 (L. Frumer ed. 1982).

80. *Bass*, 646 S.W.2d at 768. The Missouri Court of Appeals did not rule on the issue of *res ipsa loquitur* because the court determined that the plaintiff failed to make a submissible case under the physical injury rule. *Id.* at 766 app.

81. *See, e.g.*, Critcher v. Cleveland, C., C.& St. L. R.R., 132 Mo. App. 311, 111 S.W. 891 (1908) (first Missouri decision to apply a true impact rule although not by name); Trigg v. St. Louis, K.C. & N. Ry., 74 Mo. 147 (1881); Oblatore v. Brauner, 283 F. Supp. 761 (W.D. Mo. 1968); Williams v. School Dist. 447 S.W.2d 256 (Mo. 1969); Langworthy v. Pulitzer Publishing Co., 368 S.W.2d 385 (Mo. 1963); McCardle v. George B. Peck Dry Goods Co., 191 Mo. App. 263, 177 S.W. 1095 (1915); Chawkley v. Wabash Ry. Co., 317 Mo. 782, 297 S.W.2d (1927) (en banc).

82. *Bass*, 646 S.W.2d at 768-72.

83. *See supra* notes 41-42 and accompanying text for a list of the three justifications for the impact rule's existence.

84. *Id.*

85. *Bass*, 646 S.W.2d at 769. *See supra* notes 9, 15-16.

86. 436 Pa. 401, 261 A.2d 84 (1970). *See supra* note 41 and accompanying text. The *Niederman* court relied heavily on the rule in Falzone v. Busch, 45 N.J. 559, 214 A.2d 12 (1965), in deciding to abandon the impact rule. The court in *Niederman* decided that it was not sufficient to precipitate the old impact rule in the name of precedent and liability should be extended to provide redress for substantial wrongs, including injury resulting from mental distress. *Niederman*, 436 Pa. at 402, 261 A.2d at 86.

lawyers to prove, or for judges and jurors to understand the causal connection, these complications are insufficient to prevent the plaintiff from bringing his case before the court or jury.[87]

Judge Welliver, in his dissent, disagreed with the *Bass* majority's reasoning with regard to the causal connection argument and instead adopted the Missouri Court of Appeals rationale.[88] The court of appeals decision stated in relevant part that although society has become complex and automated, "[a]utomatic devices and mechanical contrivances are not foolproof"[89] and mechanical or electrical malfunctions often cause fear. Judge Welliver argued that there is no constitutional or legal right to a life free from worry, upset, or mental distress; and some unpleasant occurrences must be tolerated without resort to the courts for redress.[90]

The majority in *Bass* also rejected the contention that the impact rule is necessary to prevent fraudulent claims.[91] Echoing other courts' reasoning,[92] the majority determined that the integrity of the judicial system rests upon the notion that the courts must "find ways to solve problems, not avoid them."[93] The court relied on the decision of *Falzone v. Busch*,[94] which stated in pertinent part, "a court should not deny recovery for a type of wrong which may result in serious harm because some people may institute fraudulent actions."[95] The *Bass* court agreed with the *Falzone* reasoning that courts could guard against insufficient claims through the rules of evidence and requirements of the sufficiency of the evidence; therefore, the impact rule's purported usefulness is without basis.[96]

The dissenting judge again disapproved of the majority's reasoning and focused on the subjective and unforeseeable nature of damages for mental distress unaccompanied by physical impact or con-

87. *Bass*, 646 S.W.2d at 769. The *Bass* court quoted Niederman v. Brodsky, 436 Pa. 401, 261 A.2d 84 (1970), and adopted the language set forth in that decision.

88. *Bass*, 646 S.W.2d at 774. Judge Welliver, in his dissent, argued that the case was not transferred "because of its failure to follow the law, but because of the desire of members of this Court to change the law." *Id.* He then suggested that the court adopt the Missouri Court of Appeals decision which he attached to his dissent as Appendix A. *Id.* Because Judge Welliver adopted the court of appeals' decision on his own, discussion of the dissent focuses on that decision.

89. *Id.* at 777.

90. *Id.* at 777-78.

91. *Id.* at 770.

92. *See supra* notes 29, 30 and 42 and accompanying text.

93. *Bass*, 646 S.W.2d at 770.

94. 45 N.J. 559, 214 A.2d 12 (1965).

95. *Id.* at 563, 214 A.2d at 16. The *Bass* court did not follow the decision set forth in *Falzone*, but merely adopted that court's repudiation of the impact rule. The *Falzone* court allowed recovery if the requirements of the zone of danger rule were met. *See supra* notes 50-56 and accompanying text.

96. *Bass*, 646 S.W.2d at 770 (*quoting* Falzone v. Busch, 45 N.J. 559, 563, 214 A.2d 12, 16 (1965)).

temporaneous physical injury.[97] Judge Welliver relying on Missouri case law,[98] asserted that damages for emotional distress are based on guesswork and should be denied because such damages may be punitive in nature.[99] He also concluded that the reasonable man cannot be expected to anticipate and guard against these remote injuries emanating from the minds of plaintiffs in the absence of an initial physical injury or impact.[100]

Finally, the *Bass* majority declined to conclude that the impact rule is necessary to prevent the alleged flood of litigation which might ensue if the judicial system permits claims for emotional distress without proof of impact or initial injury.[101] The court noted that jurisdictions that have abandoned the impact rule have not suffered a barrage of litigation.[102] The majority concluded, as have other jurisdictions which have abandoned the impact rule,[103] that it is "the duty of the courts to afford a forum for the remedy of wrongs."[104] Judge Welliver, in a strong dissent on this point, stated that a flood of litigation would result, with disasterous results.[105] Judge Welliver reasoned that new courts would be needed to relieve overcrowded dockets; existing high liability insurance premiums would rise; and businesses planning to locate in Missouri would have to take the increased costs into consideration.[106]

Although the *Bass* majority criticized the rigid limitations inherent in the impact rule, the court did determine that some type of limitation on recovery for mental distress had to be imposed.[107] The court considered the standard set forth in the Restatement (Second)

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97. *Bass*, 646 S.W.2d at 778-79 app. *See infra* note 100.

98. *See* supra notes 77 and 81. *See also* Francis v. St. Louis Transfer Co., 5 Mo. App. 7 (1877); Connell v. Western Union Tel. Co., 116 Mo. 34, 22 S.W. 345 (1893); Warner v. Southwestern Bell Tel. Co., 428 S.W.2d 596 (Mo. 1968); Brisboise v. Kansas City Public Serv. Co., 303 S.W.2d 619 (Mo. 1957) (en banc); Pretsky v. Southwestern Bell Tel. Co., 396 S.W.2d 566 (Mo. 1965).

99. *Bass*, 646 S.W.2d at 779 app. The dissent reasoned that damages originating in the mind of the claimant are subjective and esoteric in nature, and therefore, are not calculable under conventional standards. The damages would be punitive, but punitive damages are not to be awarded in cases involving negligence, as opposed to intentional or malicious conduct. *Id.*

100. *Id.* at 779-80 app. Physical impact does not necessarily result in contemporaneous physical injury, but courts use these terms interchangeably. Often courts also interchange the phrases "impact rule" and "physical injury" rule. *See, e.g., Bass*, 646 S.W.2d at 776 app. Rarely will a plaintiff who suffered impact and resultant emotional distress be denied recovery under either rule simply because he did not suffer initial bodily injury at the time of impact. *See supra* note 29.

101. *Id.* at 770.

102. *Id. See supra* notes 28-30 and accompanying text.

103. *See supra* notes 28-30, 46-49, 52-56, 59-73 and accompanying text.

104. *Bass*, 646 S.W.2d at 770.

105. *Id.* at 774 app.

106. *Id.* This is an example of the stance taken by jurisdictions that are reluctant to extend the zone of liability in mental distress cases. Under this posture, these courts emphasize the economic well-being of the state over the redress of individuals who suffer from severe disabilities. *See supra* note 23.

107. *Id.* at 772.

of Torts,[108] which delineated a distinction between mental and physical injury, but declined to adopt it.[109] The court reasoned that the rule set forth in the Restatement (Second) of Torts was merely "the replacement of one arbitrary, artificial rule [the impact rule] with another which [is] only somewhat less restrictive."[110] The *Bass* court based this determination in part on the decision in *Todd v. Goostree*,[111] in which the Missouri Court of Appeals abandoned the distinction between physical and mental injury in workman's compensation cases.[112] The *Todd* decision indicated both the impending abandonment of the impact rule, and the Missouri Supreme Court's growing realization that the distinction between physical and mental injury is virtually impossible to establish.[113]

Based upon both logical and practical considerations, the *Bass* court abandoned the classic impact rule as well as any requirement that "physical injury" result from the emotional distress.[114] The *Bass* court adopted as its new standard a liberal approach predicated upon both the foreseeability and the severity of emotional or mental distress. The California Supreme Court first set forth this liberalized standard in the frequently cited case of *Molien v. Kaiser Foundation Hospital*[115] and stated that a plaintiff may be able to recover for negligently inflicted emotional distress unaccompanied by impact or consequential physical injury provided that three tests are met: the

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108. RESTATEMENT (SECOND) OF TORTS § 313(1) (1965) states:

> If the actor unintentionally causes emotional distress to another, he is subject to liability to the other for resulting illness or bodily harm if the actor
>
> (a) should have realized that his conduct involved an unreasonable risk of causing the distress . . . and
>
> (b) from the facts known to him should have realized that the distress, if it were caused, might result in illness or bodily harm.

RESTATEMENT (SECOND) OF TORTS § 436(1) (1965) states:

> If the actor's conduct is negligent as violating a duty of care designed to protect another from a fright or other emotional disturbance which the actor should recognize as involving an unreasonable risk of bodily harm, the fact that the harm results solely through the internal operation of the fright or other emotional disturbances does not protect the actor from liability.

RESTATEMENT (SECOND) OF TORTS § 436A states in pertinent part:

> If the actor's conduct is negligent . . . and it results in such emotional disturbance alone, without bodily harm or other compensable damage, the actor is not liable for such emotional disturbance.

109. *Bass*, 646 S.W.2d at 771-72.

110. *Id.* at 771. *See supra* notes 57-58 and accompanying text.

111. 493 S.W.2d 411 (Mo. App. 1973).

112. *Id.* In *Todd*, the plaintiff-employee suffered severe emotional shock after he discovered the crushed body of his fellow worker beneath the wheels of his truck. The court favored recovery and reasoned that disability resulting from shock, fright, or other emotional stimulus is "accidental or personal injury" within the requirements of the Workmen's Compensation Act. This decision effectively abolished the distinction between physical and mental injury in workman's compensation cases in Missouri.

113. *See supra* notes 46-58 and accompanying text.

114. *Bass*, 646 S.W.2d at 772.

115. 27 Cal. 3d 916, 616 P.2d 813, 167 Cal. Rptr. 831 (1980). *See supra* notes 66-73 and accompanying text.

plaintiff's mental injury must be reasonably foreseeable to the defendant, imposing upon the defendant a duty to refrain from or prevent the hazardous conduct or occurrence; the plaintiff's emotional distress must be "serious" in that an ordinary person would be unable to cope with the incident and would succumb to distress;[116] and either the circumstances of the case must establish a guarantee of a genuine claim or the plaintiff can introduce "medically significant evidence of serious emotional distress."[117] In the final analysis, the Missouri Supreme Court applied the new standard to the facts of *Bass* and determined the questions for retrial to be whether the defendants could foresee that an ordinary person would succumb to serious emotional distress resulting from confinement in an elevator, and whether plaintiff's emotional distress was sufficiently severe to be legally cognizable.[118]

Bass is the first Missouri case to hold that a direct victim of a negligent act may recover for mental distress or emotional suffering absent impact or consequential physical injury. The court's analysis reflects the ever-present tension in the tort law between two theories of recovery. One theory, which states that "for every wrong there should be an available remedy" directly conflicts with the struggle to limit liability. The *Bass* court renounced the arbitrary and unjust results that ensue from attempts to clearly delineate the limits of liability; however, public policy dictates that some limits must be imposed. The *Bass* decision abandoned the most conservative rule, the impact rule, and adopted the most liberal standard to date. It is ironic to note that before *Bass*, large recoveries were granted for trivial impacts and resulting mental distress, while no recovery was allowed for serious emotional harm, sometimes accompanied by grave physical disability, absent impact. The rule in *Bass* then clearly ameliorates the impact rule. Although courts find it difficult to devise a rule for emotional distress cases that is both equitable and unclouded by ambiguity, *Bass* indicates that someday the standards in this controversial area of the tort law will reflect positive societal changes and will become more clearly defined with time.

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116. *See supra* note 68.

117. *Bass*, 646 S.W.2d at 772-73. Judge Donnelly filed a short dissent in which he argued that the circumstances of the case were not appropriate for judicial abrogation of the "impact rule." The question surrounding the abandonment of the impact rule "seems suited for legislative action." *Id.* at 781 (*quoting* Epple v. Western Auto Supply Co., 557 S.W.2d 253, 254 (Mo. 1977) (en banc)). Judge Donnelly, criticizing the majority's adoption of a "medically significant" rule, stated, "[t]he logic and 'practicality' of such action elude me. What does 'medically significant' mean in a courtroom?" *Id.*

118. *Id.* at 773-74. The court noted that if a possibility of proof exists that the plaintiff has not fully developed, remand is permissible. *See, e.g.*, Franklin v. Farmers Mut. Ins. Co., 627 S.W.2d 110 (Mo. App. 1982); Bolhofner v. Jones, 482 S.W.2d 80 (Mo. App. 1972). [Casenote by Linda J. Cowell]